

State Brownfield

Insurance Programs, 2004

Northern Kentucky University

University of Louisville

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Executive Summary

Increasingly over the past five years, state environmental agencies and economic development departments in the US have explored the potential of state-led brownfield insurance programs to help manage the risks of brownfield cleanups and redevelopments. For the past year, Northern Kentucky University and its partner the University of Louisville have studied the experiences of existing state insurance programs and chronicled the efforts of other states to examine the value of and, in some cases, to establish such programs. The overall intent of this report is to offer information to stakeholders and decision-makers about these activities to help them assess state-assisted environmental insurance as a brownfields tool.

The findings reported here derive from several sources. These include in-depth interviews with representatives from state brownfield programs and the insurance industry; focus groups with state insurance program staff and other brownfield stakeholders; field notes from educational and policy-making meetings, workshops, and conferences; and documents gathered from Web searches and provided by state government personnel.

The report begins with an introduction to the types of insurance products that currently are in use or being considered for state programs:

- *Pollution Liability* (PL) policies provide protection for the costs of third party bodily injury or property damage claims arising from pollution conditions, legal expenses to defend against these claims, and first party cleanup costs and other expenses caused by pollution.
- *Cost Cap* (CC) policies protect against cost overruns that arise in the conduct of a planned site remediation. At present, the policies are not available in the open market for projects with expected remediation costs of less than \$1 million.
- *Secured Lender* (SL) policies provide reimbursement to lenders in the event that a borrower defaults and a pollution condition exists on the property held as collateral.

Three states that have made the greatest effort in terms of state insurance programs are described in detail in the first three chapters.

- **Massachusetts** established the oldest state program in 1999, the Brownfields Redevelopment Access to Capital (BRAC) program. It provides pre-negotiated, low-cost insurance policies to those who borrow funds to regenerate brownfields and to lenders who finance the projects. The state subsidizes premium costs to a maximum of \$25,000 for PL coverages plus \$25,000 for CC coverages. Premium prices are provided in pricing schedules that are renegotiated every two years. Cost reductions for premiums result from use of the pre-negotiated policies that save the insurer policy tailoring expenses and from volume discounts offered by the insurer by virtue of being the single provider for the program. The policies also facilitate lender willingness to loan on brownfields by protecting a borrower's capacity to service a loan and providing lenders with

funds to remediate a site should a foreclosure become necessary.

The results of BRAC in terms of job creation and development expenditures leveraged are substantial according to state analysts. Currently, BRAC personnel are engaged in scheduled renegotiations with insurers. They face unresolved dilemmas in terms of selecting an insurer or insurers due to the fact that SL and CC policies are not offered by all carriers that are interested in participating in the BRAC program.

- **California** is in the process of developing its Financial Assurance and Insurance for Redevelopment (FAIR) program. FAIR is modeled after BRAC, but no funds are available for subsidies. Although legislation for the program was approved in 2001, FAIR developers predict that the program will not begin before the end of 2004.

Delays in implementation can be traced to two main factors. First, the specificity in the enabling legislation placed limitations on the program. The bill required the California Environmental Protection Agency (Cal/EPA) to use a competitive bidding process to select an insurer or insurers, mandated detailed elements of insurance products, and required development of a strategy to encourage participation by multiple insurers. Negotiations with the provisionally selected insurer also have been delayed by the bill because it requires terminology inconsistent with insurance policy language and necessitates provision of policies for all brownfield cleanups. Second, a change of administration in California resulted in a reevaluation of the state's brownfields action plan as a whole and interrupted the insurance program negotiations. Current paramount concerns on the part of FAIR developers include providing cost-effective CC coverages for small-scale brownfields, funding program administration, and verifying policy discounts to be offered by the insurer.

- **Wisconsin** personnel are involved with an existing program that protects state funds when natural attenuation of groundwater is used as a remedy at a brownfield site and with a new program under development, the Wisconsin Brownfields Insurance Program (WBIP). Like BRAC and FAIR, the proposed program is intended to offer reduced-price, pre-negotiated policies. State subsidies are not a program component, although the state occasionally will loan or grant EPA Brownfields Cleanup and Revolving Loan Fund monies to subsidize insurance. PL and CC policies have been requested from insurers.

WBIP's development has proceeded relatively rapidly. This progress may be attributed to the work of a team consisting of Wisconsin's Department of Natural Resources, a state environmental insurance broker selected through a competitive bidding process, the state risk manager, and the Brownfields Study Group, an organization created several years ago by the legislature to provide policy recommendations for brownfield redevelopments.

WBIP's developers are now in negotiations with several insurers. Issues to be resolved include how program evaluation data will be collected, the extent to which discounts offered by the

insurer will be sufficient to attract developers, whether or not the program will be able to offer premium pricing schedules, and the extent to which pre-negotiated policies will adequately fit the needs of individual brownfield projects.

In addition to these three states, others have been engaged in efforts to develop or investigate state insurance programs. The review of these states in Chapter 5.0 points to the need for information dissemination and communication among state representatives.

- **Connecticut** has a program that offers subsidies for brownfield insurance to those who borrow money from state funds. However, there has been no demand for the insurance due to the extensive site assessments that are conducted on the sites in order to access state funds.
- **Pennsylvania** has introduced a bill that would establish a state insurance program modeled after BRAC and FAIR. Subsidies would be included and funds already have been set aside for this purpose. The pending legislation is almost identical to California's FAIR legislation. The extent to which the Pennsylvania bill will be revised to avoid the problems California encountered as a result of the FAIR legislation remains to be seen.
- **Colorado** has been involved in the last year in an exploration of state insurance programs. The Colorado Brownfields Foundation, a partner in this research team, formed an Environmental Insurance Steering Committee. The Committee held stakeholder discussions to explore the feasibility and desirability of a state program and organized subsequent conference calls with insurers. At this point, participants believe they will not pursue a program that involves use of extensive resources. This decision was based primarily on the perception that Colorado is not in a position to offer subsidies and on the fact that affordable CC coverages are not available for small sites, which are a priority in the state. Committee members now are discussing the possibility of offering a program that would provide education about environmental risk management at brownfields, including insurance.
- **Delaware, Rhode Island, Vermont, and Virginia** brownfield personnel were given legislative or gubernatorial mandates to investigate ways to make affordable brownfields insurance available. Beyond researching the issue, the states have not taken further action to develop a program, although they are still pursuing the possibility.
- **Indiana and Wyoming** also have initiated efforts to research the potential of a state insurance program, but have not reached conclusions at this time.
- **Florida and Minnesota** investigated the concept of a state program, but decided against pursuing one. Minnesota's investigation was cursory with respect to insurance; the decision was based largely on one focus group discussion. Florida's conclusion was based on an informal survey. The primary reasons for deciding not to pursue a program were similar to Colorado's, i.e., lack of funds for subsidies and lack of affordable CC coverages for small sites.

The final chapter of the report discusses key concerns and considerations raised in prior chapters and offers the following conclusions and recommendations.

- ***Determining the impact of environmental insurance*** on private investments is extremely difficult. A recent study of developers indicates, however, that insurance assistance is likely to be part of the stimulus mix that is needed to attract developers to brownfields.
- ***The nature of insurance products*** as they are currently offered causes consternation on the part of state representatives.
 - *Affordable CC coverages* are not available for small-scale cleanups. Within a state insurance program framework, no solution to this problem has been found.
 - *PL policy terms* have become shorter than in the past. While this is problematic, there are advantages to purchasing shorter terms and renewing a policy, i.e., lower premium prices may be available if no large claims on the policy have been filed before renewal.
 - *SL policies* increase lender willingness to loan on brownfields. Depending on specific policy provisions, however, they may have negative impacts on the likelihood that adequate site assessments will be conducted and the likelihood of cleanups occurring if a borrower defaults. The BRAC program now uses an endorsement to a borrower's PL policy that transfers the policy to the lender on foreclosure. Compared to the ways in which some SL policies are written, the endorsement improves the probability that a cleanup will occur.
- ***Even if subsidies are not offered***, there are benefits to a state insurance program, including PL pricing schedules that help developers assess the feasibility of projects, pre-negotiated policies that save the insured legal expenses and time tailoring policies, and reduced costs of premiums. Considerations pertinent to establishing a program that does not include subsidies are examined.
 - *Pre-negotiated policies*. Those planning state insurance programs need to be aware that pre-negotiated policies still will require modifications to fit the needs of individual sites. Some modifications will be initiated by the insurer to limit coverages because of particular problems at a site. At times under a state program, the insurer may find it necessary to refuse coverage altogether for an especially risky project.
 - *Price reductions*. While insurers maintain there are price reductions under state programs, they do not permit access to their books to confirm the reductions. At present, verification of discounts can only be gathered from the reports of brokers and clients who seek policies from insurers outside of a state program before entering the program.
 - *Attracting enough projects*. Some state representatives fear that their states may not have enough brownfield projects to achieve volume discounts from an insurer. Although this may be the case in some states, in others the concern may be exaggerated. Volume can be

generated by program marketing that brings more smaller developers into the brownfields marketplace. Also, the volume that carriers anticipate comes from within and outside of the program, i.e., selection of a carrier as a state provider helps the insurer in marketing efforts and facilitates sales outside the program.

- *The impact on premium cost reductions of using a single versus multiple providers* is impossible to determine at this time. Furthermore, given the state of the insurance market, in which some insurers have ceased to offer CC and SL coverages, it is difficult to envision how a multiple-insurer program could be structured.
- *Lessons regarding developing a state insurance program* can be drawn from the experiences of Massachusetts, California, and Wisconsin.
 - *Legislation* that establishes a program must be flexible to allow for changes in the insurance market.
 - *Using a broker* to negotiate with insurers and assess the merits of their proposals is more efficient than placing state officials in the broker role.
 - *Program administration* functions including marketing and evaluating a program should be addressed early on in the program creation process.
 - *A multiple stakeholder team* that includes individuals with a variety of areas of expertise is optimal for program development. Wisconsin's team provides a good example.

The brownfields insurance market is constantly evolving. Evidence of this is provided in a proposal from one insurer for a new, untested approach to state programs described in the final chapter.

Annual revisions of this report are planned for the next four years, through 2008. A number of issues that are undetermined in this report will be resolved by the next edition.

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Chapter 1.0

Introduction and Methods

Brownfields were defined in federal law for the first time by the 2002 Small Business Liability Relief and Brownfields Revitalization Act.¹ They constitute “...real property, the expansion, redevelopment, or reuse of which may be complicated by the presence or potential presence of a hazardous substance, pollutant, or contaminant.” Public sector efforts to address those complications have, however, been underway since the breadth of the contaminated land problem was recognized in the 1980s.

The states have played a major role in brownfield policy innovation. During the past five years, state brownfield personnel have explored the potential of state-led insurance programs to help manage the risks of brownfield cleanups and redevelopments. The 2002 Act prompted additional interest in this approach by allowing federal funds to be used for insurance purchases.

The Office of Brownfields Cleanup and Redevelopment of the US Environmental Protection Agency (EPA/OBCR) signed a Cooperative Agreement with Northern Kentucky University (NKU) in 2003 that included in its five-year work plan the preparation of annual reviews of state activities with respect to state brownfield insurance programs. This is the first of those reviews.

NKU, with its partner the University of Louisville, spent the past year studying the experiences of existing state-level insurance programs and chronicling and providing technical assistance to states in the process of establishing such programs. Investigations by other states to explore the merits of a state program also were documented. The intent of this report is to offer information to brownfield stakeholders about these activities to help them examine the different ways they might include environmental insurance in their brownfield toolboxes.

Open-ended interviews and focus groups were conducted with public officials, insurers, brokers, and others to collect data on the many considerations involved in creating a program, the factors that facilitate or impede program development, and the ways in which those barriers have been or potentially could be overcome. The authors also participated directly in Colorado’s deliberations about insurance, working with the Colorado Brownfields Foundation, another NKU project partner.

The current report builds on three earlier NKU reports the authors prepared for EPA/OBCR on environmental insurance and brownfields, all of which are available on the EPA Brownfields Website:

- *Environmental Insurance Products Available for Brownfields Redevelopment, 1999* (2000) summarized brownfield coverages commercially available as of late 1999.²

¹ <<http://www.epa.gov/brownfields/sblbra.htm>>

² <<http://www.epa.gov/swerosps/bf/pdf/insrep99.pdf>>

- *Environmental Insurance and Public-Sector Brownfields Programs: Factors Affecting Pursuit of Insurance as a Redevelopment Tool* (2000) documented public entity efforts to develop insurance programs and summarized the difficulties they encountered.³
- *Models of Government-Led Brownfield Insurance Programs* (2002) assessed the viability of various models of local and state-led insurance programs for multiple brownfield sites.⁴

1.1 Research Methods

Any study of public policies and programs that are evolving as they are reviewed has to start with a snapshot at a point in time. Since this report is intended to review the processes by which the policies are formulated as well as the end results, the research methods employed required on-going monitoring as well as production of summary findings. Repeated interviews with individuals were combined with focus group sessions, direct participation in ongoing deliberations, and data collection from state Web pages and other documentary materials. Returning to similar sources in future years will make it possible to develop a picture of changes over time.

Interviews. Interviewees included representatives of state economic development units and environmental agencies and insurance carriers and brokers. Interviews were free-flowing conversations tailored to individual interviewees. Most all were tape recorded and transcribed, and quotations are used to elaborate issues raised. In order to encourage free expression of ideas and opinions, interviewees were assured that they would remain anonymous. Where quotes are used, only the state to which each comment refers is noted; the names and organizational affiliations of individuals are not revealed.⁵

Focus groups. Colorado provided the major source of focus group data. The Colorado Brownfields Foundation organized the sessions for diverse sets of stakeholders in order to determine their priorities for state-level provision of brownfields liability relief and to see how insurance could serve those objectives. Additional focus group sessions were held with managers of state insurance programs from California, Massachusetts and Wisconsin to encourage reflection on their programs in light of experiences in the other two states.

Direct participation. The authors participated in a range of educational and policy-making sessions including workshops, meetings, and conferences. These activities entailed a higher degree of active involvement than is typical in participant observation studies: the researchers provided information and opinion at the same time as they collected data from those involved in state efforts. Activities

³ <<http://www.epa.gov/swerosps/bf/pdf/meyeryou.pdf>>

⁴ <<http://www.epa.gov/brownfields/pdf/nku2002.pdf>>

⁵ Note that editorial liberties were taken with the interview quotes to make them flow smoothly. For example, false starts to sentences were omitted, intervening phrases and sentences that confused meaning were eliminated, ambiguous pronouns were clarified, and so on.

included presentations at state, regional, and national workshops and conferences, some of which were organized by EPA; technical assistance training conducted by the authors for state personnel; and academic conferences at which state insurance programs were discussed. In addition to tapes of the sessions, field notes from these activities were recorded for analysis.

Documentary research. Web searches were conducted to identify states interested in brownfields insurance. State Website content was reviewed extensively for studies and other information about the use of insurance or program involvement with insurance risk transfers. Reports and guidance materials were downloaded and examined in detail. Additional documents used for this report were collected from other presenters at conferences and workshops the authors attended.

1.2 Overview of Brownfield Insurance Products

In order to appreciate the motivations and expected impacts of the efforts of different states to promulgate brownfield insurance programs, it is necessary to understand the types of insurance policies most relevant to brownfield redevelopers. Insurance allows investors to manage risks and uncertainties by transferring them to insurers. Beyond the uncertainties associated with any real estate investment, brownfields pose two major exceptional risk exposures. The first involves costs for site assessments, mitigation responses, and remediation activities. The second entails environmental liabilities associated with possible harm done by pollution to occupants of a property, to adjacent properties and their occupants, and to the local environment as a whole.

Three classes of coverages in use or under consideration for state programs address these risks. The summaries below are intended to provide the minimum information needed to follow the policy discussions in subsequent chapters. More detailed descriptions are provided in the *Products Available, 1999 (2000)* study and the *Models (2002)* study referenced above. An update on the insurance coverages available will be prepared in 2005.

Unlike standardized coverages such as automobile insurance, brownfield policies are highly ‘manuscripted’ or customized to address the unique risk management issues of each project. Carriers often include ‘endorsements’ or contractual modifications that waive exclusions or provide additional coverages needed.

The listings below summarize types of coverage that ***might be*** contained within specific policies; the actual coverage will be the result of manuscripting negotiations, depending on the carrier and the particular brownfield project. Please note that the descriptions are intended to communicate meaning to readers who are not in the insurance industry. They generalize across very specific, legally binding terms used in actual policies and so should not be relied upon when purchasing insurance.

1.21 Pollution Liability Policies

The most widely sold category of insurance coverages is referred to here as Pollution Liability (PL). Various PL products have been offered for over twenty years, but the availability and scope of coverages expanded greatly in the past decade. The policies provide protection for costs that result from ‘legacy’ issues or preexisting pollution conditions (either unknown contamination or known pollution conditions disclosed at the time a policy is written). In addition, they protect against costs arising from current site conditions (accidental releases that occur during the policy period).

The risks covered may be categorized into three basic components. The first consists of protection for the costs of ‘third party’ claims arising from a pollution condition. The second provides protection for ‘first party’ cleanup costs and other expenses related to pollution. The final element is for legal defense costs associated with the first two components. Each of these requires a brief explanation.

- *Third party claims* refer to legal efforts either seeking damages from, or action by the defendant and alleging legal responsibility for damage. Third parties may include private parties *and* government entities enforcing environmental regulations. The damages may occur onsite or offsite (on locations beyond the boundaries of the insured property such as nearby properties where pollution has migrated, hazardous materials disposal sites, and properties damaged during transportation of contaminants). Claims may be made for (a) bodily injury; (b) property damage including, in some policies, diminution of the value of property; (c) offsite remediations; and (d) other expenses related to a pollution condition such as business interruptions during a cleanup.
- *First party coverages* protect the insured against its own costs resulting from any onsite remediation required, including remediation of previously unknown, preexisting pollution and current pollution from ongoing operations. Other first party coverages that may be purchased entail protections against business interruption and ‘soft’ costs due to project delays caused by unexpected contamination such as income loss. ‘Re-opener’ coverage is available to protect an owner against the costs of actions ordered by state environmental regulators that reopen a project case under state laws after having previously approved the cleanup.
- *Legal defense* costs associated with the first two elements can be substantial. The policies generally indicate that the carrier has both the right and the duty to defend the insured against those who claim either monetary damages or a need for contamination remediation. The costs of such defense are included in the policy dollar limits.

Currently, policy periods of one to five years are typical, but it is possible to buy a ten-year policy. It is important in this regard to understand that PL policies are ‘claims made and reported’ policies. This means that for the coverage to respond, a claim must be made against the insured and reported to the insurer during the policy period.

1.22 Cost Cap Policies

The second type of brownfields insurance, referred to here as ‘Cost Cap’ (CC), protects against cost overruns that might arise in the performance of a remediation plan. The insurer pays the excess costs above a ‘self-insured retention’ (SIR), a term that can be confusing because it is used in two different ways. At times, the SIR is meant to refer to the estimated cleanup costs *plus* a ‘buffer’ or amount that the insured is obligated to pay before making a claim. At other times when insurance representatives use the term SIR, they are referring only to this buffer. In this report, the terms buffer and SIR are used synonymously,

The SIR is typically calculated as a percentage of the estimated cleanup cost. Thus, for example, on a planned \$1 million remediation with a 10% SIR, the policy ‘attaches’ (starts paying for costs) after \$1.1 million – the estimated cost plus \$100,000 – has been spent by the insured. A policy may include a co-insurance provision under which costs that exceed the SIR are shared by the insurer and the insured in a predetermined ratio.

The specific coverages that may be provided with a policy, depending on the carrier and specific mitigation project, include costs due to the following:

- Discovery of a greater volume or higher concentrations of “known” contaminants;
- Discovery of new or “unknown” contaminants;
- Changes in regulatory requirements during the performance of the remediation plan;
- Project delays caused by unexpected contamination, including income loss and debt service costs incurred during the delay.

The coverages depend heavily on the details of the remediation plan and estimated costs, which must be approved by the insurer. The policies generally specify exclusions such as unwarranted contractor delays and changes in the cleanup plan that have not been approved by the carrier. They are generally written for the length of the anticipated duration of the remediation, but may include a few additional weeks or months. Typically, long-term operation and maintenance costs, such as pumping and treating groundwater over a period of years, are not included.

One issue regarding CC that recurs throughout this report concerns provision of the coverages for sites with ‘small’ planned cleanups. The statistical data base that individual carriers used in the 1990s to price CC coverages was small due to the newness of the policies. Some insurers undercharged for the policies and experienced losses. The most dramatic losses were incurred on smaller projects for which adequate site assessments were not conducted. Because the costs of conducting adequate assessments would make the policies cost-ineffective, insurers made the decision to not offer CC policies for sites with estimated cleanups under \$1 million or \$2 million, depending on the insurer.

1.23 Secured Lender Policies

Unlike the first two types of coverage, Secured Lender (SL) policies do not protect developers or owners; they are intended to benefit lenders. They contribute to brownfield redevelopment activity by making lenders more willing to provide capital. In general, creditors are concerned about a borrower's ability to repay a loan if a project encounters unanticipated cleanup costs. Lenders also worry that a drop in collateral property market value due to contamination may keep them from recouping the loan in the event of a foreclosure.

SL policies, which emerged in the mid- to late-1990s, protect a lender in the event that a borrower defaults and the default is accompanied by a pollution condition. In some policies, the default must be caused by the pollution. Specific coverages that may be provided, depending on the carrier and project include:

- Reimbursement for the lesser of the cleanup costs or the principal loan balance, so that the lender either has full collateral value on which to foreclose or the loan repaid.
- Cost of third party liability claims for bodily injury, property damage, diminution of property value, and business interruption resulting from contamination.
- Legal defense costs to defend against third party claims.

As in the case of CC policies, there has been a retraction of SL coverages in the insurance industry due to losses carriers have incurred. At present, only two insurers offer the policies. The impact of this retraction is discussed in the following chapter on Massachusetts. Chapter 6.0 examines other problematic aspects of SL policies, including their impact on the likelihood of a cleanup occurring at a site if a borrower defaults on a loan.

1.24 Other Coverages

State programs promoting insurance as a brownfields stimulus focus on the three types of policies above. However, there are other insurance coverages relevant to contaminated land mitigation efforts.

- ***Finite Risk programs.*** Although Finite Risk programs (also called Blended Finite Risk) include a CC component in that the insurer pays excess cleanup costs above a buffer, they are structured quite differently in that some or all of the funds expected to be needed for a cleanup and other costs are paid at the outset of the program. The approach involves a profit-sharing arrangement between the insurer and the insured on the returns earned by investment of the deposited funds. Because the program concept is based on investment income over time, the Finite Risk approach is appropriate for brownfields where cleanup costs are expected to be high, remediation is expected to take at least five years, and extensive site assessments have been conducted.
- ***Service provider coverages.*** Insurance companies have developed products for businesses exposed to liabilities stemming from their involvement with pollution conditions. Contractors' Pollution Liability policies cover contractors that handle remediation, demolition, transportation

and disposal of hazardous materials. They protect against third party property damage, bodily injury, and environmental cleanup claims. Errors and Omissions policies provide protection against claims for mistakes and negligent acts for environmental engineers, lawyers, consultants, laboratories, and other professionals providing services and advice.

- ***Owner-Controlled policies.*** To help property owners avoid having to make sure all their contractors and professional consultants have coverages needed, insurers offer Owner-Controlled insurance programs to cover pollution conditions caused or exacerbated by the operations and services of all contractors and consultants working on a project.

1.3 Report Overview

This report opens with three chapters devoted to the most advanced states in terms of insurance program development. Chapter 2.0 addresses the experiences and current operations of Massachusetts' Brownfields Redevelopment Access to Capital Program. Chapter 3.0 is devoted to California's Financial Assurance and Insurance for Redevelopment Program and its efforts to negotiate program provisions with the selected underwriter. Chapter 4.0 reports on a state program already in place in Wisconsin and a new insurance program the state currently is developing.

We then turn to experiences in other states, including Connecticut's support for developers wanting insurance assistance, Pennsylvania's pending legislation, and other state legislative and gubernatorial mandates to investigate insurance. Reports on states that have launched investigations of insurance are included, highlighting the activities in Colorado and discussing two states that made the decision not to pursue an insurance program at this point in time.

The report closes by discussing key issues that emerge from the examination of state insurance program efforts. Insurance is examined as one of a broad array of possible state brownfield incentives. Concerns expressed about the programs are then addressed, including problematic aspects of CC, PL, and SL products. The subsequent section of the chapter discusses issues relevant to state insurance programs that do not offer subsidies. This is followed by a comparison of program development processes in Massachusetts, California, and Wisconsin. The report ends by emphasizing the changing nature of the brownfields insurance market and enumerating issues that should be resolved before the 2005 edition of this report is released.

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Chapter 2.0

Massachusetts' Brownfields Redevelopment Access to Capital Program

Implemented in 1999, Massachusetts' Brownfields Redevelopment Access to Capital Program (MassBRAC or BRAC) is the oldest state brownfields insurance program. The 1998 Massachusetts Brownfields Act⁶ created BRAC and designated the Massachusetts Business Development Corporation (MassBusiness) as the entity that would administer the program. MassBusiness, an economic development organization in existence since 1953, reports to the Department of Economic Development (DED).

The program provides pre-negotiated, low-cost, and state-subsidized environmental insurance policies to those who borrow funds to purchase, clean up, and/or redevelop brownfields and to lenders who finance the projects. Premium prices are provided in pricing schedules that are renegotiated every two years. Cost reductions for premiums result from use of pre-negotiated policies that save the insurer manuscripting costs, and from discounts offered by the insurer by virtue of being the single provider for the program.

There are significant benefits to BRAC users. As with all brownfields insurance, environmental risks are transferred to the insurance company, thus making redevelopment projects more economically viable. The policies also facilitate access to capital by protecting the borrower's capacity to service a loan and by providing lenders with the funds to remediate a site for sale should a foreclosure become necessary. A BRAC user saves legal expenses and time negotiating policies in addition to reduced costs of insurance. Furthermore, the pricing schedule helps a developer to calculate costs to assess the feasibility of a project.

In addition to these benefits, an advantage of CC insurance is that the insurer provides a second opinion about the quality of Remedial Action Plans (RAPs). This is particularly valuable in states such as Massachusetts that have a privatized program whereby Licensed Site Professionals conduct site assessments and remediations. While the government can audit the remediations for five years after completion in Massachusetts, a cleanup can occur without any state oversight. The insurer is an independent party whose interests are to determine that the plans will achieve remediation goals and be cost effective.

In this chapter, we present the coverages offered under the program and their costs. This is followed by a discussion of premium subsidies under the program and how they have changed with funding fluctuations. We then review eligibility requirements and application procedures, summarize the development of the BRAC program, and describe program administration procedures. The subsequent section presents the results of the program in terms of project dollars expended on BRAC projects,

⁶ <<http://www.mass.gov/legis/laws/seslaw98/sl980206.htm>>

the creation of jobs by the projects, and other benefits. Finally, as this report is submitted, MassBusiness is in the process of negotiating a new contract with insurers. We end the chapter with an overview of the decisions with which BRAC staff are contending and possible outcomes of the negotiations.

2.1 Insurance Coverages

Policies for developers include coverages for pollution liability, business interruption, and cleanup cost overruns. Each of these three can be purchased separately, for a separate premium. More specifically, the policies provide the following:

1. *Pollution Liability*

Coverage A pays:

- clean-up costs for on-site, pre-existing pollution conditions outside a RAP area and;
- legal defense, bodily injury and property damage claims related to pre-existing, on-site pollution conditions.

Coverage B pays:

- third party claims for cleanup of off-site, pre-existing pollution conditions and,
- legal defense and off-site bodily injury and property damage claims by third parties related to pre-existing pollution conditions.

2. *Pollution Liability - Business Interruption* (Coverage C) pays actual loss, or loss of rental income and extra expense, for business interruption related to pollution conditions.

3. *Cost Cap*

- Coverage D pays clean-up costs for pre-existing *known* pollution conditions within a RAP area that exceed the estimated cost of cleanup (as determined by the insurer).
- Coverage E pays clean-up costs for pre-existing *unknown* pollution conditions within a RAP area.

The term limit for PL policies is five years. Typical of all brownfields insurance, they are ‘claims made and reported’ policies, i.e., a written claim must be made against the insured and reported to the insurer during the policy period or extended reporting period. A sixty-day automatic extended reporting period is provided. The insured also is entitled to purchase an optional extended reporting period endorsement of up to forty months.

In addition to these protections, an insured may buy coverages by endorsement (or policy modification) for a variety of provisions such as policy renewal, increased term and dollar limits, and for various risks such as discovery of new conditions and natural resource protection. However, the costs for these endorsements may not qualify for the state subsidy if they do not conform to the intent of BRAC’s enabling legislation. In particular, the legislation was not designed to address future releases of contamination. So, for example, coverage for potential leaks of an underground storage tank could be added to a policy, but the resulting increase in premium price would not be subsidized.

In the past, BRAC also offered a separate SL policy for lenders. In June of 2004, however, the program's insurer stopped offering the policy altogether. Although no losses were incurred from BRAC policies, losses from SL policies issued outside the BRAC program led to the carrier's decision to withdraw from the SL market. (Discussion of the status of SL coverages and the consequences of utilizing specific SL policy provisions is provided in Chapter 6.0.)

At present, protection is offered to lenders through BRAC in two ways. First, the PL policy protects the borrower if an unexpected remediation is required and/or a liability suit is filed against the borrower. Whereas these events might otherwise jeopardize the borrower's ability to service the loan, the insurance would pay for these costs up to the policy limit and allow continued payment on the loan. Second, if a lender should need to foreclose on a loan for which the brownfield property is held as collateral, the lender can be protected by a 'mortgagee/insured assignment' endorsement that automatically converts a borrower's PL policy to the lender. This assures that funds will be available for environmental cleanup so that the property can be sold. Furthermore, during remediation and before the site is sold, the lender has the benefit of protections from third party bodily injury and property damage claims and coverage for legal expenses.

2.2 Insurance Costs

The following tables provide examples of the costs of insurance as of the fall of 2004 pricing schedules. Prices for Coverages A and B vary with the limits and deductibles selected. Note that the policy term is five years and that the figures reflect the cost of insurance *before* the subsidy. As noted in Table 2.2, additional discounts apply for PL coverages if CC insurance is purchased as well. The mortgagee assignment endorsement can be added to a borrower's PL policy at little or sometimes no additional cost.

Table 2.1. Examples of Current Pollution Liability Premiums for Coverages A and B				
Policy Limit	\$10,000 Deductible	\$25,000 Deductible	\$50,000 Deductible	\$100,000 Deductible
\$500,000	\$5,032	\$4,780	\$4,528	\$4,276
\$1,000,000	\$9,642	\$8,386	\$7,715	\$7,128
\$5,000,000	\$30,086	\$28,235	\$25,456	\$23,143
\$10,000,000	\$44,125	\$41,409	\$37,336	\$33,942

Table 2.2. Examples of Current Pollution Liability Premiums for Coverages A and B With Purchase of Cost Cap Insurance				
Policy Limit	\$10,000 Deductible	\$25,000 Deductible	\$50,000 Deductible	\$100,000 Deductible
\$500,000	\$4,193	\$3,983	\$3,773	\$3,563
\$1,000,000	\$8,035	\$6,988	\$6,429	\$5,940
\$5,000,000	\$25,072	\$23,529	\$21,213	\$19,286
\$10,000,000	\$36,771	\$34,508	\$31,114	\$28,285

Table 2.3. Examples of Premiums for Coverage C: Business Interruption	
Policy Limit	Premium
\$500,000	\$1,190
\$1,000,000	\$1,980
\$5,000,000	\$5,475
\$10,000,000	\$6,982

The pricing structure for Coverages D and E is somewhat more complicated since two Self-Insured Retention (SIR) options are offered. Premiums for both options are shown in Table 2.4. Again, the pricing is before the premium subsidy. Projects with estimated cleanup costs in excess of \$800,000 receive a 5% discount from the insurer's standard cost, or the amount an insured would be charged for the coverage if it were purchased on the open market.

Table 2.4. Examples of Current Cost Cap Premiums: Coverages D and E					
Estimated Cleanup Cost	Policy Limits	SIR	Premium	SIR	Premium
Up to \$100,000	\$100,000	35%	\$22,778	50%	\$19,361
	\$300,000	35%	\$39,444	50%	\$33,527
\$700,001- \$800,000	\$800,000	10%	90% Std Cost*	20%	80% Std Cost
	\$2,000,000	10%	90% Std Cost	20%	80% Std Cost

*Std Cost: the insurer's standard cost, which are not noted on the pricing matrix.

BRAC representatives estimate that program participants have received a 30% to 50% reduction in insurance premium costs before the subsidy. No systematically collected data are available, however, to verify the volume discounts for premiums. For proprietary reasons, the BRAC insurer does not permit MassBusiness personnel access to their books. Although contractually, MassBusiness has the right to utilize an independent auditing firm to review the carrier's pricing, they have not chosen to do so because, first, they would prefer to expend funds on insurance for brownfields rather than for consultant fees. Second, to confirm price reductions, they have collected information comparing BRAC prices with prices for policies outside the program from brokers and borrowers who obtained estimates before entering the BRAC program.

One problematic issue with respect to pricing in the BRAC program and in other state programs merits discussion here, i.e., providing cost-effective CC coverages for small-scale brownfield projects. For reasons discussed in Chapter 1.0, most insurers will not offer CC coverages for projects with cleanups of less than \$1 to \$2 million, depending on the carrier. Because of the volume of business anticipated from the program, the BRAC insurer has been willing to insure these smaller projects. The cost for the coverage, however, is prohibitive. For example, for a \$100,000 expected cleanup, with policy limits of \$100,000 and a 35% SIR, the premium without a subsidy would be \$22,778. This means that an insured party would have to spend \$57,778 above the estimated cleanup costs (the premium plus the SIR) before the policy would begin paying. Even with the Massachusetts 25% subsidy of the premium cost, the developer would still pay \$52,083 above the estimated costs.

In an effort to encourage lower premium prices, BRAC staff offered to develop a fund that would guarantee the insurer a certain amount of losses on small-site CC policy claims. However, BRAC's current insurer and other insurers now negotiating with program personnel have declined the offer:

MA Rep: We've offered inducements in the form of establishing loss reserves on their behalf so that they could use some of the fund assets to pay portions of the losses under the Cost Cap program. We asked, what will that do for you in terms of being able to lower the price so people can afford it? We said we would put \$1 million in an escrow account they could draw out to pay the first Cost Cap losses for sites with cleanups under \$500,000 or even \$1 million. They said no thank you.

One insurer who rejected the concept argued that the approach would not be feasible in terms of obtaining legislative support for funding. That is, the proposal would not be politically palatable to legislators because, while the insurer would collect premiums and benefit from good experiences, the state would be asked to protect the insurer from losses.

The need for CC insurance for small projects is a theme that runs through subsequent chapters. At present, the problem remains unresolved for state insurance programs. The issue is discussed further in Chapter 6.0 where an approach to the problem is offered that entails a portfolio of small sites owned by a single entity such as a local government.

2.3 Subsidies under BRAC

Funding for BRAC has fluctuated since 1999. The 1998 legislation provided \$15 million for the program, but in January of 2003, over \$7 million of the funds remaining at the time were appropriated in an effort to balance the state's budget. In early 2004, however, \$6 million were returned to BRAC.

The responses to these fluctuations provide insight into MassBusiness and DED personnel perceptions of priorities for stimulating brownfield redevelopments. Before the 2003 reductions, BRAC users received a 50% subsidy of their premiums and there were no per-project limits on the amount subsidized. Approved policy endorsements that increased the cost of a policy – such as longer policy periods – qualified for a subsidy. When the budget became precarious in 2003, BRAC dropped the subsidy to 25% of the costs of premiums for all coverages and limited the total per-project premium subsidy to \$25,000.

When funds were restored in 2004, a decision was made *not* to reinstate the original 50% subsidy; the consensus was that this percentage had been too generous, especially in light of the fact that there was not a substantial drop in interest in the program when subsidies were reduced. However, the maximum project limit was increased to \$25,000 for PL coverages (A, B, and C combined) plus \$25,000 for CC coverages (D and E combined). Subsidies for most policy endorsements now are allowed except for coverages for new releases from ongoing operations, since such coverages do not conform with the BRAC legislation, and for longer policy terms due to the costs of the endorsement:

MA Rep: We don't pay for extension of policy term or for adding new conditions coverage. For almost any other endorsement, we will pay. The longer policy periods can drive the cost up considerably. If you double the term from five to ten years, you might triple the cost of insurance. We'll pay for an automatic renewal provision and revisit the project five years later if they want to renew, but we don't pay that premium up front.

While BRAC personnel have established limits in order to address as many sites as possible, the legislation does not actually place percentage limits on premium subsidies or on the total amount subsidized per project. A party may apply for higher subsidy funding through an appeals process. Case-by-case determinations are made based on environmental and economic criteria:

MA Rep: In order to obtain greater than the 25%, \$25,000 per policy limit, you need to appeal to us and the state makes the final determination. We have done that a handful of times. There are no established criteria; applicants just have to make a strong case that there is a significant public benefit associated with the project and that, if not for the assistance, the project might not be able to move forward. The public benefit can be in terms of job creation in an area hard-pressed with respect to employment. It can be cleaning up a really dirty site that's a threat to the health and welfare of citizens. The few that have been granted exceptions all have had a number of elements that were very positive.

2.4 Eligibility and Application Procedures

As a basic eligibility requirement, BRAC applicants must borrow capital for some aspect of their brownfield project because the BRAC legislation was intended to facilitate financing. Exceptions to this rule are made for some municipalities and non-profit redevelopment authorities that, for example, receive funding from grants. A private developer that does not borrow funds, however, may be eligible to obtain discounted insurance, but not the premium subsidy.

For eligibility purposes, brownfields are defined as vacant, abandoned, or underutilized real properties where expansion, redevelopment or reuse is complicated by real or perceived environmental contamination. Because the concept of *perceived* contamination can be subjective, classifying a site as a brownfield can be problematic:

MA Rep: Where we've wrangled with some potential users has been with the notion of *perception* of environmental contamination. Basically, if a site has a history of documented releases - even one and it's been remediated - then the perception of contamination can still linger and we would allow the site into the program. If there's a high probability of contamination based on prior or current use, we'll put it in the program.

No needs test is required to receive BRAC assistance. For the most part, however, the financing requirement and the limits on total subsidy tend to exclude large site developers that would purchase insurance without state assistance:

MA Rep: When you get into projects that involve multimillion dollar cleanups, they're often companies that don't really need the assistance. The thinking is, if you need to get financing, you're not a Fortune 500 company. Other than financing, there's no other needs test, but we've weeded out some of the larger projects just by having the financing requirement.

To participate in the program, a borrower or a borrower's broker submits to the insurer a BRAC application and all site assessments. CC insurance also requires a RAP, Scope of Work and cleanup cost estimates. Copies of the application and the conclusion sections of the assessments are sent by the borrower or broker to MassBusiness. MassBusiness then notifies the insurer and the broker upon determining the borrower's eligibility. The insurer and the broker negotiate the coverage, determining endorsements that may be needed for a specific project and the insurer issues a quote for the insurance, a copy of which is sent to MassBusiness. When the applicant and insurer have agreed to the terms and conditions of the insurance, the insurer issues a binder and submits a copy to MassBusiness. The broker notifies MassBusiness when the premium payment has been sent to the insurer. After the applicant completes a BRAC premium subsidy questionnaire, the insurer issues the policy and MassBusiness issues a subsidy payment to the applicant. Note that no application is required for the mortgagee/insured assignment endorsement; a BRAC applicant simply requests that it be added to a PL policy.

It is the intention of BRAC personnel to remain as unobtrusive as possible in the interactions among the borrower, broker, and insurer, while at the same time, collecting data that assures the carrier is offering coverages at the scheduled pricing and allows MassBusiness to assess program results:

MA Rep: We try to stay out of the way. We ask the applicant or broker to provide a copy of the application form which is a one-page, two-sided informational document and a copy of the environmental information on the site. That's all we ask for going in. Based on that information, 99 percent of the time, we can qualify a site for the program. The original paperwork goes to the insurance company and they begin the underwriting process as soon as they get it. Once we qualify a site, we simply email the underwriter so they know they can price it based on the BRAC pricing. Then they just undertake the normal underwriting process. The only thing they do differently is copy us when they issue a quote for the coverage so we can check the pricing to make sure it conforms with our schedule. When coverage is bound, we have a questionnaire we ask people to complete. It's only seven or eight questions about their project and their financing. When we get the questionnaire back, we issue the subsidy check. The typical turnaround time on a PL is two weeks from the date the insurer receives the application and the environmental information to the date they render a quote for coverage. One of the comments I've heard fairly repeatedly is that we do a great job of not getting in the way of the normal process.

2.5 Program Development

The origins of BRAC are interesting, in that it was not originally intended as an insurance program. Rather, the legislation envisioned BRAC as a loan guarantee program for brownfields, modeled after the state's Capital Access program, a small business economic development program whereby lenders charge an eligible borrower up to three points on a loan. The state then matches the points collected and the total is placed into a reserve for the bank to pay for loan losses. The BRAC legislation, however, limited the program's guarantee to funding for environmental assessments and remediations. This approach was impractical with respect to brownfields financing since few banks provide loans solely for those purposes; usually, funds for site assessment and cleanup are made as a part of larger packages that also finance the purchase and development of a site. Consequently, only a small portion of the bank's total loan would benefit from the BRAC guarantee, making it of little use. Because the program could not function as intended, MassBusiness staff reexamined the legislation to seek a more practical application. As the legislation permitted the fund to be used to purchase insurance to protect borrowers and lenders from loan losses from environmental conditions, an insurance program was conceived.

No open competitive bidding for the insurance contract was needed since MassBusiness is a private corporation rather than a state agency. Massachusetts also has a procurement statute that exempts the purchase of insurance from the state's normal bidding process. Thus, MassBusiness personnel were able to investigate insurance providers, select the company they believed was best, and begin negotiations. The selected insurer was chosen because of its financial strength and longevity in the

market. In addition, other carriers would not commit to a predetermined pricing schedule, would not provide CC, or would not provide CC for small-scale brownfield projects.

The insurance policies were developed by the insurer, MassBusiness, the DED, and the Commonwealth's Attorney General's office. Expenses incurred by the state included MassBusiness and DED time and expenses and some \$250,000 in legal fees to review the pre-negotiated policies.

2.6 Program Administration

The work of MassBusiness staff consists of qualifying applicants, issuing subsidy payments, maintaining program databases, publicizing BRAC, providing educational outreach about the program, and managing negotiations with insurers every two years. The cost to administer the program is \$345,400 per year on fixed-price contract that includes direct costs related to the program, overhead, and salaries for 2.5 FTEs.

Maintaining a data base for program evaluation purposes is essential to continued public support for BRAC. Data provided by the insurer include the amount of dollar limits and premiums for policies and claims payment records. Information from the insured is collected from the one-page premium subsidy questionnaire. Subsidy payments are not issued until the completed questionnaire is returned to MassBusiness. Information requested includes:

- the cost of environmental cleanup at the site;
- the total amount expended for purchase and development of the site;
- prior and proposed use of the insured property;
- estimates of the number of permanent jobs retained and created as a result of the project,
- the source and amount of financing used for the purchase, environmental assessment, remediation, and development of the site, and;
- the means by which the user learned about BRAC.

2.7 Results

The results of BRAC are impressive. With support from the program, numerous sites that had been idle for years are now productive or ready for reuse. One municipal project, for example, involved a large, abandoned manufacturing site. The town had been working with responsible parties to arrange a settlement agreement for several years when the negotiations fell apart due to disagreements about who should pay if unknown contaminants were to be discovered in the future. A \$10 million PL policy, subsidized by BRAC, resolved the issue and the site has now been remediated. In another instance, BRAC supported a project on a two-million-square-foot abandoned site that had not been generating taxes for years. The town now has a facility projected to produce approximately \$1 million a year in tax revenues for the community and to create 2,000 jobs over the next five years.

Table 2.5 provides MassBusiness' statistics for BRAC from its inception in October of 1999 through August 17, 2004. As indicated, with \$4.6 million in subsidy payments, BRAC facilitated environmental cleanups of more than \$140 million and encouraged development expenditures after cleanups of \$1.8 billion.

Table 2.5. BRAC Program Results October 1999 - August 17, 2004	
Number of projects in program	232
Insurance dollar limits provided	\$879,886,500
CC \$40,500,000	
PL \$653,000,000	
SL* \$186,386,500	
Insurance premiums charged	\$10,983,233
CC \$1,737,057	
PL \$8,359,652	
SL \$886,524	
Subsidies paid	\$4,655,669
Cleanup costs expended	\$140,157,124
Jobs created or retained	24235
Created 17,459	
Retained 6,776	
Total development expenditures	\$1,829,343,988
Loans \$1,088,331,550	
Investment \$741,012,438	

*SL policies were discontinued by the carrier in June 2004.

Although a number of the BRAC policies were written in recent years and policy holders may yet file claims, to date, there have been nine claims made under the program. All claims have been promptly paid with no contention from the carrier. This positive record may be indicative of the insurer's standard operating procedure. It also may be an artifact of the carrier's high visibility as the insurer for a state program:

MA Rep: Every one of the claims was paid without dispute, generally within ninety days of being made. Could this be because it's a state program and we ask them to report this information? The fact that we are a state program and we generate quite a bit of business might have something to do with it. I know at least one of those claims was borderline and the insurer might have been justified in disputing it, but they just paid it. They didn't ask any questions. Our experience is we haven't had a single complaint, but of course, we haven't had that many claims.

2.8 2004 Insurer Negotiations

The contract with the BRAC insurer ended in July of 2004. Earlier that year, MassBusiness issued a Request for Information (RFI) or expressions of interest in becoming the carrier for the program. As this report is written, MassBusiness is in the process of negotiating with three insurers. While the negotiations continue, the arrangement with the original carrier has been extended until the end of 2004. As indicated in Table 2.6, MassBusiness faces important trade-offs in selecting an insurer, as the three carriers have offered different coverages and conditions.

Table 2.6. BRAC Contract Negotiations, 2004			
	Offering PL	Offering CC	Offering SL
Carrier A	Yes But wants limits on yearly amount	Yes But not for cleanups under \$1 million	Yes But adverse to high risk sites and wants limits on yearly amount
Carrier B	Yes	Yes	No
Carrier C	Yes	No	Yes

While Carrier A offers all three types of coverages, their proposal has important limitations. First, the insurer has so far declined offering CC policies for projects with cleanups under \$1 million – a critical restriction, since CC coverages for small-scale sites is a central program goal. Second, the insurer is reluctant to offer SL policies on sites where there is a good possibility of contamination that might lead to a claim:

MA Rep: They told us they don't write Secured Creditor on dirty sites. And I said, well, we have a brownfields program. If our sites are not known to be dirty, at the very least they have a propensity to have issues. So we've had further discussions with them and I think brought them to the point where they'll look at sites that have issues, but not outright cleanups needed.

Finally, Carrier A would like to place limits on the dollar amounts it would provide for PL and SL coverages each year:

MA Rep: The biggest stumbling block is they want to put limits on how much insurance they will write under each type of insurance in any year. In other words, they would write Secured Creditor, but will only do up to \$50 million in a year. And in years gone by, we've done well in excess of that. And they had similar limitation on Pollution Liability. They said they would write \$100 million, but last year we did \$128 million in Pollution Liability, and we can't put the program in the position of only offering \$100 million and then having to wait until the next year to offer more.

The option of having a carrier provide only CC or SL was explored, but was found to be untenable because PL is preferred by all three providers:

MA Rep: What all the carriers really want is the PL coverage. They don't want to do the lender coverages under this program and they don't want to do small Cost Caps. The first thing we asked (Carrier A) and (Carrier C) was, how would you like to just offer Secured Lender? They both said no thanks. It's an all or nothing proposition for both of them.

Thus, in mid-negotiations, two possibilities exist. First, BRAC may retain the current provider. While officials are holding out the hope that the carrier may decide to offer SL just for the BRAC program, a likely outcome would be to continue with the mortgagee endorsement to the borrower PL policies. This would satisfy the mandate of the program's enabling legislation to facilitate brownfields financing, but the question of whether or not the endorsement would provide adequate assurances from the perspective of lenders is still unanswered. To address this issue, BRAC personnel have prepared a short questionnaire for distribution to lenders that have participated in BRAC in the past to determine the adequacy of the endorsement. In addition, they are holding preliminary discussions the Massachusetts Bankers Association to explore the possibility of a self-insurance fund for brownfield loans. This option, however, would require turning to the legislature for additional funding.

Given that no insurer is willing to offer CC or SL without providing PL, the second possibility is to have all three carriers as providers for the program, thus instituting insurer competition into the program by having at least two insurers quoting for the same product. There are challenges, however, with this arrangement that lead BRAC personnel to prefer a single-carrier model. First, Carrier A would need to be willing to lift the per-coverage totals for SL and PL, be less risk adverse with respect to offering SL coverages, and be willing to provide CC for small projects. Second, the structure would have a negative impact on cost reductions, since the carriers would undergo the expense of underwriting projects for which no sale would be made:

MA Rep: The problem we're going to have is the insurers would have to agree that they would offer some level of discount from their standard pricing, but it would not be as significant as what we have today. We're talking maybe a 10% or perhaps 20% discount.

Finally, to allow customers to compare prices, the policies must be uniform across carriers and the two carriers that have not written policies to conform to Massachusetts' law would have to do so. These conditions require substantial legal review by the state and the insurers:

MA Rep: The problem is that we have to get three companies to agree on policy language in certain instances and things like agreeing to Massachusetts' law and certain definitions and what not. So getting them all on the same page in terms of the insurance they're writing is a major task. It would mean huge negotiations.

The BRAC program has enjoyed considerable political support within the Commonwealth of Massachusetts, particularly in the state legislature. After BRAC lost funding in early 2003, the legislature passed an economic development bill in November of that year that reinstated \$6 million to the program. The Governor, however, vetoed \$3 million of these funds. In response, the House and Senate voted almost unanimously in early 2004 to override the Governor's veto, thus restoring the \$3 million to BRAC.

In addition to support in Massachusetts, BRAC has generated substantial interest in other states. Indeed, a good portion of MassBusiness personnel time is spent responding to requests for presentations about the program to other government entities throughout the country. We turn now to California, where legislation designed to establish a state brownfields insurance program based on the Massachusetts model was passed.

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Chapter 3.0

California's Financial Assurance and Insurance for Redevelopment Program

In 1999, the California Environmental Protection Agency (Cal/EPA) began conceptualization of a program modeled on BRAC called the Financial Assurance and Insurance for Redevelopment (FAIR) program. Like BRAC, FAIR is designed to lower the costs of environmental insurance by providing a package of pre-negotiated, standardized brownfield policies and offering subsidies for the premium costs. At present, however, funds for subsidies are not available due to the state's budget constraints. For this and other reasons addressed below, the program has not yet been implemented.

Chapter 3.0 provides an overview of the FAIR program and development process. We examine the origins and content of the legislation that enabled the program. This is followed by discussion of the challenges Cal/EPA has encountered in establishing it, including impediments that have arisen during negotiations with the provisionally selected insurer in terms of accommodating both the insurer and the statutory requirements. We end with a brief discussion of current concerns on the part of Cal/EPA personnel.

3.1 Program Beginnings: Enabling Legislation

FAIR was conceived by Cal/EPA when California had a significant budget surplus in 1999. It was intended as part of California's Urban Cleanup Initiative that also included Cleanup Loans and Environmental Assistance to Neighborhoods (CLEAN), a program designed to provide low-interest loans and grants for the investigation and cleanup of brownfields. Because the insurance proposal was not as fully developed as the loan proposal, the two components were separated. CLEAN was put into place in 2000. SB 468, the enabling legislation for FAIR, was approved in 2001.⁷

Unlike the legislation that established BRAC in Massachusetts, the California statute was intended to create an insurance program. In an attempt to assure that the bill would contain mandates that insurers could accommodate, the major brownfields insurers were consulted when the bill was written. The language in the legislation is quite specific with respect to the insurance products to be provided. It mandates that PL, CC, and SL coverages all be offered and requires certain minimum elements of these coverages:

Cost overrun insurance must provide for the following:

- The response costs in excess of the estimated response action costs approved by the insurer.
- A policy period of sufficient length to cover the duration of the response activities.
- A SIR amount not to exceed 25% of the estimated response action.

⁷ http://www.leginfo.ca.gov/pub/01-02/bill/sen/sb_0451-0500/sb_468_bill_20011007_chaptered.html

Pollution liability insurance, covering damages caused by a preexisting and unknown pollution conditions from or at a site, must provide for the following:

- A minimum policy period of five years.
- A duty to defend and pay for defense costs up to the amount of coverage available under the policy.

Secured lender insurance must provide for the following:

- Response costs at a site incurred by the lender after a borrower default or foreclosure that occurs as a result of a pollution condition at the site and costs reasonably necessary to remediate the site for its intended use so that it can be sold.
- Damages or other liability for a pollution condition at a site incurred by a lender as a result of that lender exercising a foreclosure option.
- Loss or damages incurred by a lender as a result of a borrower's inability to satisfy a loan obligation or due to the existence of an unforeseen and unexpected pollution condition.
- A duty to defend and pay for defense costs in an amount at least up to the amount of coverage available under the policy.

To support innovative effort, the legislation also permits the Secretary of Cal/EPA to authorize any other insurance products for brownfields to be eligible for subsidy support.

SB 468 requires the Secretary to solicit proposals through a competitive bidding process in a manner consistent with the requirements for state procurement of services. It specifies that only insurance companies rated by AM Best as having a Financial Strength Rating of A+ or better and a Financial Size Category of FSC X or larger are eligible.⁸ The legislation left open the possibility that more than one insurer would be selected. The insurance company or companies chosen would be assured that they would be the exclusive state-designated provider(s) of environmental insurance for a period of three years.

The bill authorized subsidies of up to 50% of premium costs and up to 80% of the SIR for CC policies to a maximum of \$500,000 per project. Loss of funds for these subsidies was the first major setback for the program. When CLEAN was put in place in 2000, it was funded for \$85 million and, at that time, Cal/EPA anticipated that an additional \$37 million would be awarded for FAIR. Eventually, however, even remaining CLEAN funds reverted back into the general fund, and, in the end, only \$500,000 from the state was designated for implementation of FAIR. This was supplemented by an additional \$200,000 from federal EPA funds. The decision was made to continue development of the program, however, hoping that use of pre-negotiated policies and the anticipated volume discount offered by the carrier(s) would make the program valuable to brownfield developers.

⁸ A Financial Strength Rating of A+ or A++ means 'Superior;' the top two grades on a thirteen-point scale. A Financial Size Category of FSC X or larger means that a policyholder surplus is available for claims coverage of \$500 million or more.

3.2 Request for Proposals and Qualifications and Responses to the Request

Because Cal/EPA personnel did not have professional backgrounds in environmental insurance, a consulting firm was brought in to help prepare and evaluate responses to the Request for Proposals and Qualifications (RFPQ).⁹ To prepare the RFPQ, the firm organized five workshops in the spring of 2002. The first two involved government entities such as economic development departments and regional water boards. Invitees for the third included private state associations of attorneys, bankers, real estate agents, etc. At that point, the preliminary RFQP was drafted. The last two workshops, held in Sacramento and Los Angeles, were open to the public and attracted some 250 people from a variety of backgrounds who were asked to critique the Request.

The proposal component of the Request was quite detailed. It specified provision of CC, PL, and SL coverages. Required information about the products included premium pricing schedules, indication of time needed to bind coverages, and a list of 19 policy terms and conditions such as time limits, triggers, standard endorsements and exclusions, assignment of policy to subsequent owners, extended reporting periods, and cancellations. In addition, the request called for applicants to provide a structure for the program in terms of the involvement of a single or multiple providers. Suggestions were made for multiple-provider structures such as utilization of a lead insurer that would be re-insured by other carriers and multiple preferred providers designated for FAIR that would compete with each other for policy placements.

The degree of specificity in the RFPQ was due to the mandates in SB 468 for particular insurance products and a competitive bidding process suited for procurement of services, and the emphasis among key legislators that Cal/EPA develop a strategy to encourage participation by multiple insurers within the program:

CA Rep: We didn't have a choice as far as the statute was concerned. We had to accommodate those in the legislature who felt we needed to go through a competitive process and include more than one insurer.

CA Rep: We saw that Massachusetts had some premium increases and there was always the big question mark – were those market induced changes or was there something else related to competition or lack thereof? We felt that developing a program that allowed multiple insurers could be an extremely valuable factor in trying to keep prices down. That's just the general open-market principle of competition and pricing.

CA Rep: The expectation was that we would be able to pull a rabbit out of a hat and create a system that allowed for multiple insurers. But, it's a chicken and egg situation. We couldn't specify the structure without knowing if multiple insurers were interested and nobody was

⁹ <www.calepa.ca.gov/Brownfields/documents/2002/rfqp.pdf>

interested unless they knew the program structure we would offer. So, we were in a real conundrum and we ultimately added a lot of work to our process.

The corporate size and financial capabilities mandates in SB 468 meant that there were only five carriers that qualified to compete for the contract at the time. After the legislation was passed, it became clear that subsidies would not be available. Subsequently – but not entirely consequently – insurers withdrew interest in participating in FAIR, and, as of the fall 2002 deadline for response submissions, only two insurers submitted written proposals. Two reasons account for the lack of responses to the RFPQ. First, the diminished interest was due to the removal of the subsidies, which carriers felt would have assured a certain volume of business:

Insurer: It's volume-based pricing and a volume-based commitment. We thought California certainly would produce a higher volume than Massachusetts, and then the subsidies went away and everybody lost interest.

The second reason pertained to the detailed nature of the RFPQ:

Insurer: In California they made the law way too specific about what coverages had to be and how they had to be offered. In the legislative process, you pass a law to give a general structure for approaching a situation. The regulatory actions implement that. In California, they went too far with the legislation and made it a real handicap. And the application was 33 pages long! I looked at it and said, I don't have time to do this. That was a big part of why we didn't bid.

The insurer currently in negotiations with Cal/EPA submitted two proposals – one to be the sole provider and one to participate with another carrier. In the latter case, however, no premium cost reductions were offered. Another insurer also submitted a response, offering to participate in the program with other insurers by filling a niche for small cleanup CC policies through an innovative Finite Risk program the carrier had developed. However, upper management at the firm made the decision to cease involvement in the environmental insurance market altogether and the insurer withdrew the proposal for involvement in FAIR two weeks before the end of the evaluation process.

In June of 2003, the one remaining insurer was officially selected on a provisional basis and a target date for the notice of intent to award the contract was set for October 2003. Cal/EPA began negotiations with the carrier that summer over policy terms, pricing, program administration, and the responsibilities of the state versus the insurer.

However, from the fall of 2003 to August of 2004, negotiations were interrupted, in large part, by the change of administration in California which resulted in a review of the brownfields action plan as a whole. This larger program assessment focused on complex issues including lack of coordination among the regulatory entities in California, development of an inventory of the state's brownfields, the extent of cleanup that should be required for groundwater, and the degree of immunity from re-openers that should be granted to developers when risk-based cleanups are employed.

In addition to this review, delays in program implementation stemmed from concerns raised by the insurer about the proposed program. We turn now to these unanticipated challenges with which Cal/EPA currently is contending.

3.3 Post-Selection Negotiations

Although representatives of several insurance carriers were consulted when SB 468 was drafted, most of the selected insurer's concerns stem from language in the legislation. The first pertains to the definition of a 'pollution condition:'

CA Rep: In our statute, we said that a pollution condition is a 'release or threatened release of a hazardous material.' We took the terminology directly from CERCLA and it's standard nomenclature. The definition was there when the statute was first drafted. However, the insurer's attorneys see the concept of 'threatened release' as open-ended, unbounded liability. They say any chemical that exists has a potential to release, so it's a level of threat that can't be quantified. We've gone back and forth with them on a variety of fronts, not the least of which was that they were involved at the time we enacted the statute. This language was shopped to all the major insurers to make sure that we weren't going to encounter this kind of thing, so you can imagine the frustration that now they've come back to us and said that this language is something they finding very difficult to work with. Their concern is that, although their policies don't define a pollution condition in those specific terms, if someone were to make a claim on a policy, they would revert to the statutory definition. The resolution they would like to see is a disclaimer or indemnification that the only conditions they will be obligated to cover are those found in the policies and that the statute will not supercede the policy language.

This issue is likely to be resolved by such a disclaimer. One difficulty in settling the problem, however, is the need for legal counsel with expertise in both regulatory authority and brownfields insurance:

CA Rep: In most instances governmental agencies take action based on releases and threatened releases. So the question is, how does the authority of the regulatory agencies mesh with the claims issue? We need to make sure we're not losing anything by agreeing to make an accommodation. The challenge is, our attorneys are familiar with the enforcement authorities, but there's not a lot of familiarity with environmental insurance.

A second issue raised by the carrier is that the statute requires them to provide policies for all brownfield cleanups in the state, a condition that Cal/EPA staff originally thought would bring volume to the insurer, thus contributing to the carrier's ability to offer discounts:

CA Rep: The statute says that the insurer is required to offer policies to anybody conducting a response action in the state. When we crafted that, we thought it would enhance the insurer's position, not create a negative. But they see it as creating an obligation to compete against themselves in the arena of larger cleanups. And that becomes critical, because we don't have

subsidy monies available for premiums and we're working to negotiate premium reductions. They say they're okay offering a discount to the less than \$5 million cleanups that they're not currently reaching, but they believe they're already writing policies for larger cleanups. So for them to offer a 10% discount to customers they're already insuring is giving money away. Again, this is one of those things where it would have been nice if they would have said something when we were crafting the statute. I do understand that their customers would be foolish not to take advantage of a 10% discount. The challenge is that the statute obligates the insurer to offer them insurance. So we've been trying to find ways to honor the statute, but not place the insurer in competition with itself. We've talked about only offering discounts to smaller cleanups, but offering pre-negotiated policies without discounts to larger ones.

Given this situation, an important question is whether or not the program can attract enough sites to create the hoped-for price reductions in premiums. The utility of the program to developers of larger projects remains to be seen. Policies for larger, more complex projects usually are highly manuscripted and large project developers typically have legal counsel overseeing insurance contracts. Thus they have less use for pre-negotiated policies offered under a state program.

Another complication originating from the statute is relevant to one of Cal/EPA's primary goals for FAIR – providing cost-effective CC policies for small projects. While the insurer has offered to provide the policies for projects with cleanups as low as \$100,000, there is a problem accommodating the 25% maximum SIR stipulated in the legislation. That is, a 25% SIR for a cleanup that size would require an expensive premium because insurers have concluded that the chances of overruns are greater for smaller cleanups than they are for larger cleanups. To address this, the insurer has offered a lower premium if Cal/EPA would accept a co-insurance feature to accompany the 25% SIR, i.e., the insured would agree to pay a certain percentage of the cost overruns above the 25%.

Representatives of Cal/EPA have acquired lessons that would benefit others considering a state program. These include the cumbersome nature of attempting to develop a program that utilizes multiple carriers, utilizing a competitive bidding process suited for the purchase of services for program development, and inclusion of restrictive language in legislation that establishes a program.

3.4 Unresolved Issues and Concerns

At this point, there are a number of elements of FAIR still to be determined. Providing CC coverages for small-scale brownfields has been a program goal from the beginning. Although the insurer is willing to offer them, it is anticipated that, as is the case in Massachusetts, the coverages will not be affordable. An unresolved problem also exists with respect to the legislative mandate to provide SL policies. The selected insurer no longer offers the policies, and, given the specificity in SB 468, it is unclear if a mortgagee endorsement to a borrower's PL policy, such as Massachusetts now uses, will suffice.

Other concerns pertain to program administration. Currently, there are no funds available to administer FAIR, and Cal/EPA foresees relying on a brokerage firm for this role. If performed in the ideal, these administrative functions could involve considerable effort. There is a strong desire on the part of Cal/EPA to obtain feedback from customers regarding their needs, collect data on whether or not the program is meeting these needs, and provide technical assistance to those entering the program to help them understand what protections insurance policies can and cannot provide. In addition, Agency staff are committed to monitoring the insurer's performance:

CA Rep: How do we build adequate checks into our relationship so that we have some assurance that the insurer is operating in a way that's consistent with the way we want them to operate? If we give them the seal of approval as the insurer of record for a state program, how do we assure we fulfill a consumer protection function? Otherwise, we're doing a disservice to the public.

One monitoring issue, discussed further in Chapter 6.0, involves verification of policy discounts offered under the program:

CA Rep: They're telling us we can achieve a 10% below-market price. The big question mark is, how do we know we'll be getting that discount? Premium setting is such an art and it's so highly guarded in the industry. To me, probably the most significant responsibility of program administration is assuring that we're getting what they said we would get. It's going to be the most difficult piece for us to navigate.

An unforeseen complication in regard to program evaluation is the insurer's concern that the state's request that the carrier report information for this purpose might jeopardize the insurer's standing with the Department of Insurance:

CA Rep: We want to be able to see how the program's performing and want feedback from the insureds and the insurer to get a sense of how we might make the program more responsive. The insurer sees that additional reporting as potentially exposing them to claims that they're operating as an admitted insurer in California as opposed to a surplus lines insurer and that might open them up to enforcement by the Department of Insurance.¹⁰ I think their concern is that, just by virtue of participating in this program, they would be considered an admitted carrier *de facto*, so that they would be in violation of not having filed all their papers and not having complied with all the requirements that admitted carriers are required to follow. It's still vague as to how we might address this issue in a way resolves their concern.

¹⁰ Brownfields insurance consists of 'excess and surplus lines' insurance made available when the standard insurance market does not provide needed coverages for various reasons (e.g., manuscripted policies are required). This type of insurance is offered by 'non-admitted' insurers that are not licensed in the state in which they operate. Non-admitted insurers are exempt from many regulations that apply to the standard market and are not required to file their forms and rates with state insurance departments. They are, however, subject to oversight that varies from state to state. For example, many states have laws requiring them to place business through excess and surplus lines brokers licensed by the state.

An additional and critical issue for Cal/EPA is identifying mechanisms to adequately compensate the brokerage firm that would carrying out program administration functions:

CA Rep: One of the features we're negotiating in the context of program administration is to get the insurer to agree to pay for a state broker. We would issue a RFP to hire a broker and a percentage of the traditional commission paid as part of the insurance transaction would go to the broker to administer the program on our behalf. The challenge is that the broker who would agree to operate as our agent would have to be willing to take only the commissions that are generated on sales as compensation. It's a fairly risky proposition. What if no volume comes in the first few years? So we would have to work out the details of their level of effort in the absence of commissions. That's not an insignificant challenge.

Cal/EPA hopes to have a program in place by the end of 2004. However, they hold an unassuming vision for FAIR:

CA Rep: Right now, we have modest expectations for the program. We want to get it on the books and see if we can tailor it to make it useful to a segment of brownfield developers. You get opinions across the map as to whether we should be in the business of environmental insurance. My opinion is, it can't hurt if we're not spending taxpayer money on it. As long as we can get the insurance company to invest themselves in this, it can give us another tool that we can use in California and I'm all for it. And if we can get something on the books and it's successful, we can expand it.

We turn now to Wisconsin, a state developing a program that intentionally does not rely on premium subsidies. Progress in program development in that state is moving rapidly in comparison to California. We examine the processes and personnel involvements that account for this difference.

Chapter 4.0

Wisconsin's Brownfield Insurance Programs

Wisconsin's Department of Natural Resources (DNR) is involved with two insurance programs – an existing one established in 2001 and another currently in development. The first is designed to allow the state to issue timely liability relief to developers using natural attenuation of groundwater as a remedy at a brownfield site. The second is intended to provide low-cost insurance to those participating in the state's voluntary cleanup program or those who have received a closure letter under a the state's traditional cleanup program. Conceptualization of the program began in January 2003. It is anticipated that a contract with an insurer will be signed by December of 2004.

We begin by describing the nature and origins of the existing program, then move to describe the new program and the processes involved with its development. The chapter ends with an examination of program issues that are unresolved at this point.

4.1 The Voluntary Party Liability Exemption, Natural Attenuation of Groundwater Insurance Program

Wisconsin's first program is designed to protect state funds that may be jeopardized by the role the state plays in cleanups involving natural attenuation of contaminated groundwater. Under the state's Voluntary Party Liability Exemption (VPLE) program, participants, including Responsible Parties, may be granted a transferable Certificate of Completion (COC) by the DNR. The COC is exceptionally thorough in that it assures recipients that they are not responsible for further cleanup at a site due to past releases even if environmental standards change, the cleanup action fails, or the contamination is found to be more extensive than anticipated.

To expedite redevelopments, DNR considered the possibility of issuing a COC in cases where a site owner was using natural attenuation as a remedy, but had not yet achieved the state's groundwater standards. The question then arose, who would pay for cleanup at those sites if natural attenuation were to fail after a COC had been issued? An insurance solution was developed for this problem.

Under the VPLE insurance program, a party relying on natural attenuation is required to pay a one-time fee in order to receive a COC. The fee contributes to the cost of an insurance policy that protects the state in the event that the attenuation is not effective. The state is the insured on the policy. If natural attenuation should fail and DNR chooses to file a claim because the site poses a public health threat, the state would pay a deductible and the insurer would pay the remaining amount up to the policy limit for site assessment and onsite and offsite cleanup costs. The party that conducted the original remediation would incur no further expense. At present, eight participants are utilizing the program and several others most likely will be using it in the future.

Most of the fee paid by the voluntary party pays for the state's premium, although a small amount is deposited into a fund to pay deductibles if the state should file claims in the future. The fees are based on the previous uses and the size of the insured property. If a site has had more than one former use, the highest fee is required. The fees for 2004-2005 are provided in Table 4.1.

Table 4.1 Wisconsin VPLE Insurance Fees		
Previous Use	Total Acreage	
	0 to 4.99 Acres	5 or More Acres
Residential	\$5,039	\$5,987
Agricultural	\$9,046	\$10,758
Commercial	\$9,614	\$11,397
Light Industrial	\$11,755	\$13,927
Heavy Industrial	\$15,428	\$18,293

The policy is a portfolio policy with an aggregate limit of \$10 million and sub-limits for each site of \$1 million. New sites are added as they enter the program. The policy term for each property is ten years. The per-site deductible, to be paid by the state if needed, varies according to previous uses of the site and ranges from \$5,000 to \$25,000.

One intriguing facet of the VPLE program pertains to a 'moral hazard' problem the insurer faces. In the insurance world, a moral hazard exists when an insured party has a perverse incentive to file a claim, or when their motivation for avoiding a claim is reduced. In the Wisconsin program, this applies in that the state is the insured as well as the entity that would initiate a claim. According to VPLE representatives, the insurer accepted this hazard because of the deductible the state would have to pay, and because Wisconsin regulations specify that DNR must determine that the contamination poses a threat to public health and the environment before a site can be re-opened. Consequently, re-openers are extremely rare.

The innovative VPLE insurance program was the product of a group consisting of DNR representatives, the state's insurance broker, the state's risk manager, and the Brownfields Study Group (BSG). The BSG is a stakeholder advisory group originally mandated by the state legislature. This set of participants also was instrumental in the development of Wisconsin's new insurance program, to which we now turn. In Section 4.3, we return to discuss the merits of involving such a team in the creation of a program.

4.2 The Proposed Wisconsin Brownfields Insurance Program

At present, the DNR is in the final phase of negotiating the structure of the Wisconsin Brownfields Insurance Program (WBIP) with several major insurance providers. Thus the structure that will actually be put into place is undetermined at this time. We present here the initial program specifications given to the carriers.

Like Massachusetts and California, the proposed program would offer pre-negotiated, reduced-price policies to eligible parties conducting cleanups. State subsidies, however, are not a program component, although the state occasionally will loan or grant EPA Brownfields Cleanup and Revolving Loan Fund (RLF) monies to subsidize insurance on a limited, case-by-case basis for RLF participants only.

To explain the WBIP proposal, it is first necessary to briefly describe the differences between the two cleanup programs in Wisconsin – the Traditional program and the VPLE program. Parties in the Traditional program have received a Responsible Party letter from the DNR and are legally required to investigate and cleanup known or suspected contamination at a site and/or pollution that has migrated beyond the site. Although they are not required to do so, the Responsible Party may request that the DNR provide fee-based technical assistance including review and approval of the Site Investigation (SI) and Remedial Action Plan (RAP). Whether or not they select DNR oversight, following cleanup and pending DNR approval, the Responsible Party receives a Close Out letter. The assurance can be transferred with the property. However, if additional contamination is found, the case may be re-opened and further action may be required at the site.

The VPLE process is elective, although parties responsible for contamination can participate. A participant is required to conduct a SI of the entire property and, if appropriate, nearby properties where contaminants may have migrated. Following cleanup, a VPLE party may receive a transferrable COC, pending DNR approval. Again, this certificate assures them that they are not responsible for further cleanup, even if environmental standards change, the cleanup fails, or more extensive contamination is found.

Within this framework, the WBIP specifications to insurers propose two categories of sites with risks that would be addressed through insurance. Category 1 consists of sites either in the VPLE process or sites in the Traditional program for which the Responsible Party has undertaken steps found in the VPLE program including DNR review and approval of the SI and RAP. Those in the Traditional program that have not selected DNR oversight would not be eligible for the insurance. Category 2 is comprised of sites that have gone through the Traditional closure process and have received a Close Out letter from the state, which is subject to re-openers.

PL protections would be available for both categories of sites. Coverages proposed in the specifications to insurers for Category 1 may include the following:

- Cleanup of previously unknown contamination on and/or emanating from the site (e.g. any type of contamination not the subject of the cleanup in the RAP).
- Third party claims for bodily injuries and property damage caused by known and unknown pollution conditions on and/or emanating from the site.
- Business income interruption losses, including soft costs, incurred by the insured due to the cleanup of previously unknown contamination.
- Third party claims related to pollution conditions at and/or emanating from non-owned disposal sites.
- Third party claims related to the transportation of waste material from the site during remediation.
- When the State issues a COC or Closure Letter, coverage for future cleanup of the contaminants that were the subject of the RAP (e.g., cleanup claims by third-parties, actions by the federal government, and/or re-openers by the state for non-VPLE sites).

Proposed PL protections for Category 2 sites, which would apply after DNR issues a Close Out letter, include the following:

- Coverage only for future cleanup of the contaminants that were the subject of the Closure and/or RAP (e.g., cleanup claims by third-parties, actions by the federal government, an/or re-openers by the state).
- Third party claims for bodily injuries and property damage caused by the contaminants that were the subject of the Closure and/or RAP on and emanating from the site.
- Business income interruption losses, including soft costs, incurred by the insured due to additional cleanup of contaminants that were the subject of the Closure and/or RAP on and emanating from the site.
- Third party bodily injury, property damage, and cleanup claims caused by pollution conditions emanating from non-owned disposal sites that were used to dispose of contaminants that were the subject of the Closure and/or RAP.

Other requested benefits of the PL policy may entail protections to parties beyond the named insured on the policies. These may include assignability of the policy to future owners and provisions granting additional insured status to parties such as a buyer, seller, or lender.

A range of one- to ten-year options for PL policy terms was requested. The policy dollar limits would be selected by the insured from \$1 million to \$10 million for each incident and for the policy aggregate. No deductibles or premium costs were noted in the specifications.

For Category 1 sites, coverage would begin at a point that would provide comfort for the insurer (e.g., with the state's approval of the Phase I and Phase II assessments, SI, or RAP). Coverage would begin for Category 2 sites when the application and site investigation information is submitted to the insurer.

The DNR also chose to explore CC insurance coverages, with the understanding that this may not be a feasible element of a standardized program. CC policies would be appropriate for Category 1 sites only. An endorsement automatically would give additional insured status to lenders. Coverage would begin when the state-approved RAP, cost estimates, and application are provided to the insurer. SIRs and premium costs were not indicated in the specifications to insurers. The policy dollar limits requested are provided in Table 4.2.

Table 4.2 WBIP Cost Cap Policy Dollar Limits Requested	
Estimated Cleanup Costs	Policy Limit
Up to \$250,000	\$250,000
\$250,000 to \$500,000	\$250,000
\$500,000 to \$750,000	\$500,000
\$750,000 to \$1,000,000	\$1,000,000
\$1,000,000 to \$2,000,000	Options of \$1,000,000 and \$2,000,000
\$2,000,000 to \$4,000,000	Options of \$2,000,000 and \$4,000,000

One interesting aspect of WBIP pertains to the ways in which the broker sought to reduce premium costs. In two respects, the cost-reduction logic is the same as the BRAC and FAIR programs, i.e., lower premiums would result because (a) the insurer anticipates a volume of business, and (b) pre-negotiated policies that save transaction costs would be used. In addition, the broker proposed achieving exceptional savings by using DNR's approval of SIs and RAPs as a basis for underwriting policies. In other words, the DNR's approvals would be relied upon in lieu of the insurer's engineering review of each individual site or would constitute a substantial portion of that review. As in the case of Wisconsin's natural attenuation program, this program component would rest on the trust that the insurer has in the expertise of DNR personnel. Unfortunately, as we discuss in Chapter 6.0, confirming the extent to which this approach may reduce prices may not be possible. And, as the negotiations stand now, the extent to which insurers will be willing to rely on DNR technical reviews is unknown.

The specifications were first given to seven insurance carriers in September of 2003. Four insurers submitted proposals that addressed varying aspects of the WBIP specifications. Three immediately declined; two that did so rejected the concept of preset PL pricing for brownfield projects they had not engineered themselves. The third declined due to a shortage of personnel they experienced after several of their underwriters moved to another firm.

4.3 WBIP Program Development

Table 4.3 provides a synopsis of WBIP program development in Wisconsin. Remarkable aspects of this process that distinguish Wisconsin from other states include, first, the participants involved in the process and, second, the nature of Senate Bill 472.

WBIP Program Development Process	
2002	
December	State environmental broker selected through competitive bidding process. RFP prepared by state's Department of Administration (DOA), working with DNR.
2003	
January	DNR, DOA, and broker met to discuss need for expanded insurance program.
February	Broker presented preliminary program concepts to the Brownfields Study Group (BSG).
February – September	Broker met with several insurers for informal discussions of possible program components.
April	Broker presented preliminary insurance plan to state.
April – August	Meetings held with the DNR, DOA, and BSG to discuss program specifications.
September	Broker submitted specifications to seven insurers. Three declined.
September – December	Broker met with remaining insurers to clarify VPLE process and state's needs. Data collected by DNR given to insurers including SI procedures, re-opener records, indications of volume of business the chosen carrier could anticipate.
December	Insurers met with DNR to discuss SI procedures and re-opener records.
2004	
February	SB 472, authorizing DNR to contract with insurers, introduced to Senate.
March	Initial proposals received from insurers.
April	DNR/Broker questions about proposals remitted to insurers. Senate Bill 472 signed by Governor.
August	Insurers submitted revised proposals. Negotiations continue.

4.31 Parties Involved in Addition to DNR

State environmental insurance broker: The program began with the selection of an environmental broker of record for the state who took the lead in program development. Rather than competitively bidding an insurer, brokers in Wisconsin are selected through a competitive process. The broker then goes to the insurance marketplace and places insurance policies, pending the approval of the Department of Administration (DOA).

The DOA issued a RFP for the environmental broker to (a) renegotiate the VPLE natural attenuation policy each year and (b) serve as an advisor and broker for other environmental insurance coverages. Information requested of broker applicants in the RFP included recommendations on improving the existing VPLE program, a list of the insurers with which the broker had worked, the amount of business the applicant's firm places annually, and the applicant's overall experience with environmental insurance programs.

Because the broker works on a commission basis, the state has incurred no expense for development of the WBIP program other than DNR and DOA time. As the broker noted, "The work we're doing doesn't cost anybody anything. We get paid if we set up the program, it works, and people buy insurance policies."

State risk manager. In earlier reports, the authors pointed to instances in which the failure of brownfield working groups to include risk managers who are responsible for insurance acquisition can stall the use of environmental insurance. In California, FAIR representatives hoped they would be able to rely on their state risk management office to assist in the development of the insurance program, but found that the office did not have the requisite expertise in environmental insurance.

In Wisconsin, the state risk manager, located in the DOA, has been involved in the brownfield initiative for the last decade. Because the state owned contaminated sites, he was appointed in the early 1990s to a committee designated to revise the state's comprehensive cleanup rules. The committee met for over three years. When the new groundwater standards were in place, the DNR sought ways to encourage redevelopers to use them and turned to the risk manager for assistance. Since then, he has been meeting with the BSG whenever relevant risk management issues have been discussed.

By statute, the DOA must issue and evaluate RFPs for state brokers and approve all state purchases of insurance in Wisconsin. Beyond this, however, the risk manager has been very useful. For the new WBIP program, he reviewed the insurance specifications sent to insurers and is now participating in the selection of an insurer. In early discussions of the VPLE natural attenuation of groundwater program, an alternative approach was considered in which individual owners would be required to purchase a policy. However, the risk manager, working with the state broker, conceptualized the less costly and time-consuming approach that now is in place.

Brownfields Study Group. At the direction of the state legislature, the BSG was created in 1998 to evaluate Wisconsin's brownfields program and provide policy recommendations for additional incentives to spur brownfield redevelopments.¹¹ BSG is an advisory group to DNR; DNR selects participants and serves as the group facilitator. The group consists of individuals directly involved with brownfields from a variety of backgrounds including several local elected officials, economic and environmental consultants, corporate and environmental attorneys, a university professor, and representatives of a statewide business association and a community health organization.

DNR staff maintain that the BSG is one of the most important factors moving brownfield initiatives ahead in the state. In the past five years, the BSG has made over 150 recommendations to the legislature, the majority of which have been adopted, including legislation for the VPLE and the WBIP programs. In 2000, the legislature directed the BSG to continue its efforts. Although the group currently is not officially mandated by the legislature, it is effective for several reasons:

- Because the BSG was formed by the legislature and because it has representation from respected members of both the business and environmental regulatory communities, it has considerable legitimacy among lawmakers.
- Members are knowledgeable not only by virtue of their occupations, but also because they have been meeting for several years to examine brownfield risks and mechanisms to address them.
- The BSG reports sent to the legislature represent multiple recommendations and viewpoints, offering a venue for open and substantive public policy discourse.
- Because it meets regularly, the BSG is able to provide rapid input for program development.

4.32 Senate Bill 472

In light of the difficulties encountered in California stemming from the FAIR legislation, the WBIP legislation is worth noting. In contrast to the lengthy California bill, SB 472 consists of two sentences:

292.53 Availability of environmental insurance. The department, in cooperation with the department of administration, may undertake activities to make private environmental insurance products available to encourage and facilitate the cleanup and redevelopment of contaminated property. The department of natural resources may negotiate with, select, and contract with one or more insurers to provide insurance products under this section.¹²

The purpose of the legislation was not to avoid a competitive bidding process with insurers; given the existing insurance procurement procedures in the state, this was not necessary. As one program representative noted, "It was basically to give us the legislative thumbs up to establish the program."

¹¹ <<http://www.dnr.state.wi.us/org/aw/rr/rbrownfields/bsg/>>

¹² <www.legis.state.wi.us/2003/data/SB472hst.html>

WI Rep: The concept of having the statutory authorization for the program was a recommendation of the study group about a year before with a number of other things. The group thought it made sense to have a statutory approval to set up the program.

SB 472 was introduced to the Senate in February and was signed by the Governor in April. The ease of passage was attributed by program developers to several factors including the broad content of the bill itself, the reputation of the DNR, the support of the risk manager, and the legitimacy of the BSG which had reached a consensus on the program's value:

WI Rep: As far as getting this through the legislative process, the bill was developed by the Brownfields Study Group and that group is made up a broad base of people who have a stake in brownfields redevelopment. They were supportive of the concept; no one opposed it.

WI Rep: The legislature has a track record with us on brownfields. I think we did a nice job with the voluntary party insurance. And it made a huge difference having someone as respected as the (state risk manager) at the legislative hearing. He was an advocate for us. It was good that DOA, which is our version of OMB, approved of it. And I think the nature of the statute made a difference. The devil's in the details and California tried to put all the details in the statute, whereas we were looking for the authority for DNR to put the program together. The beauty of our legislation is that it will be flexible over time, whereas California has one snapshot frozen in time. I'm not sure how their program will react to changes in the marketplace.

4.4 Unresolved WBIP Issues and Concerns

As a work in progress, there are a number of unresolved issues surrounding WBIP. In this section, we address important issues relevant to program administration and list current concerns voiced by DNR personnel.

4.41 Program Administration

Program developers foresee WBIP being privately managed by the wholesale insurance brokerage division of the state environmental broker's company. The contract for the program will be signed by the state, this firm, and the selected insurer. Thus the state expects administrative costs to be quite low. They do plan on using some EPA funds, primarily for marketing (in addition to allowing RLF loans or sub-grants to be used to purchase insurance). Unlike Massachusetts, they do not anticipate incurring legal expenses for review of the insurance policies because they will use in-house attorneys and also can rely on free legal advice from environmental attorneys in the BSG.

A number of details concerning program administration are undetermined at this time, two of which are central. The first concerns how program evaluation data will be collected and the nature of the information gathered. At present, it is assumed that the contract with the state will have provisions

for collecting information such as the number of parties who applied, the percent offered policies, the number of claims that were paid or denied, premium costs, and policy processing time. However, DNR staff would like to monitor other aspects of customer satisfaction and, although it is not planned at this time, collection of information gathered in Massachusetts from the insured such as project job creation, investment dollars, etc. would benefit the program and provide important information for other states considering a similar program. Unlike Massachusetts, where subsidy payments can be withheld if program evaluation data are not submitted, WBIP will need to request that the information be given on a voluntary basis.

The second issue pertains to the arrangement among brokers in the state with respect to WBIP. When the program was conceived, the proposal was for insurance buyers to contact their own retail broker, who, in turn, would contact the WBIP broker. The latter then would arrange for the purchase of the insurance with the insurer. The commission on the sale would be shared by the two brokerage firms. An open question is the extent to which retail brokers would be willing to promote the program if they would be sharing a commission with the WBIP broker. While the state may market the program, perhaps the best way to generate clients is to inform brokers throughout the state about WBIP. Other brokers, however, may not be eager to bring in clients if they have to share the commission with (and perhaps lose their client to) the state program broker.

This is an important issue for other states contemplating program creation. An advantage of the Wisconsin program development process is reliance on a knowledgeable environmental insurance broker to lead the effort to create the program at no cost to the state. Moreover, as conceived, the state brokerage firm in Wisconsin will be assuming program administrative functions. Brokers in other states, in all likelihood, will not be willing to undertake these tasks if they do not receive an adequate share of the commissions on insurance sales, or, alternatively, a fee for their services.

4.42 Other Current Concerns

No one insurance provider submitted a proposal that met all of the WBIP specifications submitted to the insurers. Some carriers, in fact, have indicated reluctance to formalizing the program with a written agreement. Others are balking at the concept of pre-negotiated pricing schedules and would like to offer across-the-board discounts instead. The DNR and DOA are trying to balance the differing proposals to determine which one best meets the needs of the state's brownfield customers. We end this Chapter by noting some of the most pressing concerns DNR and DOA personnel now have about the program. Note that we revisit these in our Chapter 6.0 discussions.

- *Will the discounts offered by the insurer be sufficient to attract developers?*

WI Rep: The program's really for the sites that aren't being served by the insurance market. We laugh about the middle class sites – the less-than-\$5 million sites. Hopefully, the prices will be cheap enough to get that reluctant market to step forward.

- *Will enough parties find the program useful to keep the insurer interested in the program?*

WI Rep: I hope that developers, local governments and lenders find the program to be valuable and recognize how it can really help to make transactions happen. If there's not a lot of interest and there's only a handful of sites, the insurance companies might not be interested in keeping the program going.

- *Will the pre-negotiated policies fit the needs of individual brownfield projects?*

WI Rep: My hope is that the policies won't need a lot of negotiation. In Massachusetts, even though they have standard policies, they still need to change them. But the idea here is that there shouldn't be a big need for that. If it turns out that they have to do a lot of that, it seems like it would be a lot of hassle and expense for everybody. Hopefully, the products we negotiate will meet most peoples' needs. We realize each site's different and the concerns people have vary, so we hope there aren't too many who say it's not exactly what they need and they're going to have to look elsewhere.

- *Will the program be able to provide a PL pricing schedule?*

WI Rep: One of the things we're trying to negotiate is whether the premiums are going to be fixed so that someone will know beforehand what their premium would be for a certain amount of coverage. Some insurers would like to do individual calculations for each site. It would be a big benefit to people if they knew they could get insurance for a certain amount as long as they have DNR approval. I hope that will be available.

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Chapter 5.0

Other States

The three states discussed in the preceding chapters are a subset of the states where environmental insurance programs have been considered. Others have passed legislation relating to the use of the tool, developed procedures to integrate insurance into their brownfield support efforts, or have taken steps to consider state insurance program creation.

Because a survey of all states was beyond the scope of this research project, to prepare this chapter, we sought out information from our contacts at state, regional, and national brownfield meetings and conducted follow-up interviews with staff from several states who initially contacted us for information on environmental insurance. A special focus was placed on chronicling efforts in Colorado to investigate a state program, which are described in Section 5.3. In addition, we searched the Web for any references to insurance as part of state brownfields risk management efforts and conducted follow-up telephone interviews to pursue the leads we found.

Representatives from a number of states (e.g., Nebraska and South Carolina) are quite interested in insurance, but are too short-staffed to investigate it given other brownfield program priorities. Other states (e.g., Kansas and North Carolina) exhibited no formal activity toward building a state program, other than some evidence from minutes and other Web reports indicating that they had included insurance industry representatives at meetings and conferences.

Several states funded through the 2002 federal brownfields law have decided that these resources may be used for the acquisition of environmental insurance. In a number of instances, insurance purchases are explicitly identified as an appropriate use of monies from state Brownfield Cleanup Revolving Loan Funds. Other states have included insurance premiums in expenses qualifying developers for subsidized loans or tax credits (e.g., New York). Finally, some states, such as Oregon, support lender ‘self-insurance’ and loan guarantee programs that can be used for brownfield projects.

A limited number of states have gone further than others in examining how to use environmental insurance to assist developers or their financiers in addressing the financial risks associated with environmental uncertainties in contaminated land reclamation projects. We review here the program currently operated in Connecticut, the approach to brownfields insurance under development in Pennsylvania, and the efforts of eight other states to examine the merits of insurance as a brownfield redevelopment stimulus. We conclude the chapter by describing two states that have investigated the tool, but decided against creating an insurance program.

5.1 Connecticut's Insurance Support Programs

The risk management programs in Connecticut were developed by the state's Department of Economic and Community Development (DECD), funded under its 1990 Manufacturing Assistance Act, which is intended to stimulate new manufacturing activity and ease transitions to new uses of old abandoned manufacturing sites. DECD is a funding agency, and its clients in the brownfields arena are entities pursuing reuse of previously productive sites. Roughly two-thirds of those organizations acting as site redevelopers have been local governments or their non-profit development agencies.

Two distinct programs are worthy of mention here. Both involve very close collaboration with Connecticut's Department of Environmental Protection (DEP). The first is administered within the DECD and addresses the risks of higher transaction costs and potential losses of sunk funds that characterize brownfield relative to greenfield projects. The second is intended to provide CC and PL insurance coverage when appropriate for entities engaging in site mitigation and preparation.

The *Special Contaminated Properties Remediation and Insurance Fund* provides low interest loans to assist with the investigation and cleanup of contaminated sites. Unlike many other brownfield programs, it does not address the risk of *potential* contamination: use of the Fund requires that the prospective remediator first establish that there exists *an expectation* of contamination before the loans become available. Eligibility for this support is based on a review of community and environmental impacts, as well as economic feasibility, requiring that the reuse expected should represent a tangible improvement for the local community. The Fund is basically a subsidized, below-market-rate lender to those who want to remediate a site. The loan provisions, however, contain one key risk management element: an opportunity for loan forgiveness. In the event that the assessment and remediation planning activities demonstrate that the redevelopment of a site is not economically feasible due to the expected or experienced costs of remediation, loans made under the program may be forgiven.

In July, 2001, DECD launched the *Brownfields Liability Assistance Program* offering subsidies for the acquisition of environmental insurance when needed and, importantly, support in determining the need for insurance. DECD does not offer any blanket or uniform coverage, but rather examines this need on a case-by-case basis.

That examination has tended to determine that there is little to be gained from insurance coverages for DECD projects. This situation derives in large part from how closely DECD works with DEP and the knowledge that it develops in the course of detailed site assessments on projects it funds. With DEP involved in assuring thorough site assessments, the extent of site data collection, by itself, undermines the potential value of insurance by reducing uncertainty. As one Connecticut Representative noted, "Once you evaluate a site to the Phase II and III levels, there's not usually very much that could really come back and bite you that might warrant a significant premium."

Most of DECD's clients are involved in brownfield site preparation, sometimes for a known redeveloper and sometimes 'on spec' with the knowledge that any reuse of a strategically located parcel will benefit a local community. As a result, many of the projects coming for assistance involve clearing sites and demolition, either in addition to, or in the absence of, remediation of soil or groundwater conditions.

CT Rep: What we're confronted with most, which insurance products don't cover very well, is what you may encounter during the demolition phase. So, our experiences with the insurance products are such that the exclusions are very difficult to deal with.

That is, most insurance policies do not address asbestos, lead, and other building materials issues unless those substances are found in soil or groundwater. Endorsements to add these coverages would be needed. While DECD could, in principle, assist their clients in purchasing such coverage, little demand for that form of risk transfer appears to have arisen in their experience. The absence of demand most likely is due to a combination of the public oversight that takes place with a demolition that could spread building contaminants and reliance on the remediation contractors' own insurance.

In 2003-2004, DECD engaged in an effort to advertise the availability of its insurance coverage support to local governments, development agencies, and private sector brownfield redevelopers. The Department publicized the availability of its expertise in insurance coverages and negotiations at zero cost and its readiness to subsidize a premium (up to 100% if appropriate) if it was agreed to be necessary for a party to conduct a project. The response was unexpected, in that no interested parties came forward.

State technical assistance and potential subsidies for brownfields insurance are still available, but are no longer being aggressively publicized by DECD. The Department remains interested in using the tool, but can do so only if there are clients that want to integrate insurance into their projects. As one state representative noted, "If there was evidence that this could be important in furthering our programs, I would re-institute our efforts – even if I had only one client saying they wanted to take advantage of it."

5.2 Pennsylvania's Pending Legislation

Shortly after BRAC was implemented in Massachusetts, Pennsylvania's Department of Environmental Protection (DEP) began investigating a possible state role in facilitating the provision of insurance for brownfields. A two-day workshop was held in August of 1999 with DEP staff, environmental insurers and brokers, bankers, economic development agency representatives, and brownfield insurance consultants. While the session was educational for all involved, DEP did not receive any written proposals from insurers and no concrete plans emerged from the day.

From 2000 to 2002, pursuit of an insurance program was postponed while the state participated in a study of the feasibility of a long-term stewardship trust fund. The fund was intended to manage

institutional and engineering controls on sites remediated under the state's Risk-Based Corrective Action standards. DEP expected that a state insurance program would emerge as part of the trust program, but the latter ultimately was not established.

In 2003, a new DEP Secretary encouraged the Department to work with the Department of Community and Economic Development (DCED) to develop an insurance program. HB1565 was introduced and referred to the Committee on Insurance in June of 2003.¹³ Since then, progress on passage has been delayed due to work on a major economic stimulus package that has taken precedence.

The bill proposed is based on and is almost identical to California's SB 468 that established the FAIR program. Like SB 468, the Pennsylvania bill mandates pre-negotiated insurance policies, including PL, CC, and SL coverages and contains policy specifications, including a CC SIR percentage and a minimum five-year PL policy period. Any brownfield owner or party conducting a response action would be eligible. While it also requires competitive bidding to select an insurer, the bill differs from SB 468 in specifying that a single insurer be selected as the state-designated provider for a period of three years.

As in California, the bill calls for subsidies of up to 50% of the cost of premiums and up to 80% of the SIR to a maximum of \$500,000 per project. Pennsylvania likely will avoid California's funding problem, however, since several hundred thousand dollars from DEP's 128(a) grant from EPA have been set aside to begin offering the subsidies when the program is implemented.

The discussion in Chapter 3.0 demonstrated that several of the elements listed above have proven problematic in California (e.g., detailed specifications for products such as SIRs, eligibility open to any brownfield remediator, use of a competitive bidding process, and a definition of a pollution condition in terms of a 'threatened' release.). If the Pennsylvania bill is promulgated as introduced, those implementing the state's program will face similar problems.

Since the introduction of HB 1565, representatives from DEP, DCED, and the consulting firm that advised California have met to discuss revisions of the legislation. During the discussions, some of the troubling elements were addressed (e.g., the definition of pollution condition). Another implementation barrier posed by the bill that has not been examined at this point concerns the specifications that only one insurer be selected through a competitive process and that the selected provider must offer PL, CC, and SL policies. Currently only one carrier offers all three. It remains to be seen how the experiences of California will inform future revisions of the Pennsylvania bill. Legislative action is anticipated in 2005.

¹³ <www.legis.state.pa.us/wu01/li/bi/bt/2003/0/hb1273p1565.htm>

5.3 Colorado's Investigation of a State Program

The Colorado Brownfields Foundation (CBF), a non-profit organization formed to facilitate brownfields revitalization, is a member of the research team for the multi-year project of which this report is a part.¹⁴ Thus we were able to place a special focus on Colorado's effort to explore the feasibility and desirability of a state insurance program.

In recent years, interest in environmental insurance has been expressed by members of brownfield working groups in the state, particularly in the Denver metropolitan area. The inclusion of CBF in the research team prompted the organization to form an Environmental Insurance Steering Committee (EISC) in the fall of 2003. Plans were made for stakeholder discussions to examine the state's needs in terms of managing brownfield liabilities and to explore the possibility of pursuing a state insurance program that would address those issues. To include a broad spectrum of individuals and organizations, 1,500 letters and e-mails were sent as invitation. In addition, CBF representatives attended several organization meetings to encourage participation. A special effort was made to reach out to rural communities.

Four discussion groups were held – two in the Denver area and one in a rural town in Western Colorado. A conference call also was held for those who could not attend. Despite the outreach effort, only 49 individuals participated in the discussions. These included representatives of the Colorado Department of Public Health and the Environment's brownfields program, the Colorado Department of Labor and Employment's underground storage tank program, the Colorado Office of Economic Development, local government economic development offices, EPA Region 8, environmental attorneys and engineers, municipal officials, brownfield developers and others.

Presentations were given by the project team on liability relief mechanisms, the Massachusetts and Wisconsin insurance programs, the efforts in California and Pennsylvania to establish state programs, and Florida's decision *not* to create a program (discussed below). The sessions concluded with a participant assessment of the desirability of pursuing a state insurance program. While each group addressed a range of issues, several distinct themes emerged across the groups:

- One of the primary goals throughout Colorado is facilitating the cleanup and redevelopment of small-scale brownfields. However, for individual sites with remediations of less than \$1 to \$2 million, CC insurance is not available in the open marketplace and is not cost effective in the Massachusetts program.
- Larger brownfield sites are already using environmental insurance and do not seem to require government assistance procuring it.
- Given current budgetary constraints, Colorado is not in a position to offer developers any subsidies for premium costs.

¹⁴ <www.coloradobrownfieldsfoundation.org>

- There is a pressing need for state assistance with site assessments; in relation to insurance, the assessments should take priority in terms of funding allocations.
- The time and effort of brownfield working groups might be better spent on local government efforts to resolve zoning and land use issues.
- In rural areas, the priority should be providing very basic education about problems associated with brownfields and the resources available to address them..
- Unlike states such as Massachusetts, Colorado does not have a heavy industrial past in urban areas. The state may not have enough brownfields to induce an insurer into providing volume discounts under a state program.
- The term limits of PL insurance now available are not long enough to protect against bodily injury and property damage claims associated with contaminated sites.

Of all the issues raised, the predominant conclusion was that Colorado needs help providing CC for small sites. Participants requested that follow-up discussions be held with insurance industry representatives to determine if they could address this and other issues raised.

Consequently, in May 2004, conference calls were held with six brownfield insurers. Questions from the stakeholder discussions were emailed to each carrier in advance. While the conversations focused on providing CC for small projects, other questions were addressed such as the prospects of longer PL periods in the future and whether the insurers believe Colorado has enough brownfield sites to make it attractive for a discount under a state program. The responses can be summarized as follows:

- None of the insurers offered a solution for the problem of the lack of affordable CC insurance for individual small-scale sites. However, one insurer outlined a proposal, presented in Chapter 6.0, for a PL policy appropriate for both small and large sites that provides coverages for remediation of new contamination discovered in the course of a cleanup and/or redevelopment.
- The insurers did not indicate that PL term limits would be lengthened in the future. (One, in fact, argued that the terms *should* be reduced to one year.)
- No insurer indicated that Colorado had too few brownfields for a volume discount approach. However, insurer representative comments indicated that their firms had not conducted an assessment of the brownfields insurance market in Colorado.

Following the calls, the EISC met to discuss the results and refine key issues. In October 2004, the CBF organized a state brownfields conference that included a session on insurance. One research team member presented on existing state programs and efforts to develop others. Three insurers then were asked to respond to key questions stemming from the Colorado discussions. These issues are addressed in Chapter 6.0.

At this point, EISC members are not optimistic about an insurance program that would utilize substantial resources:

CO Rep: I believe we've decided that Colorado is not the place for a significantly funded state program. We don't think there's the money, nor the leanings of the legislature to fund it. But there is excitement among members of our steering committee in terms of smaller approaches that could be taken.

The approach receiving the greatest consideration involves engaging an individual or individuals to provide education about environmental risk management at brownfields, including insurance:

CO Rep: In discussions we've had, there's a question about the role of the public sector in promoting any one private sector activity or a handful of businesses like insurance carriers. It's an age-old question for the public sector. But one role of the government is education and making people aware of options they have. And I look at the successes of Massachusetts. They direct a lot of money at a very specific solution. And you have the question, is it the right solution? Could the money be used better elsewhere? I feel better about going the direction of education and creating better access to markets that could help deals along.

Educational activities are envisioned for a variety of audiences such as local economic development offices, the real estate community, lenders, and participants in the voluntary cleanup program. Details regarding funding are undetermined. The educator(s) might be objective experts paid on a fee basis by the state or by the insurance industry or be existing employees of a Colorado state office or organization who would be trained to perform the function.

Despite Colorado's decision to forego development of an extensive insurance program at this time, the discussions about insurance have had benefits beyond exploration of insurance, most notably, educating local economic development organizations about brownfields:

CO Rep: The economic development community has tended to focus on job creation and business incentives, and not how redevelopments enable job creation and business growth. In the Denver metro area, we now have at least two county level economic developers, both of whom didn't know much about brownfields before. Now one county is considering applying for assessment grant funding and the other is inventorying sites. So I think that was tremendous.

5.4 Legislative/Gubernatorial Mandates to Investigate Insurance

The signing of the federal Small Business Liability Relief and Brownfields Revitalization Act in January 2002 created a new stimulus for state interest in insurance as a brownfields tool. Title C of the Act offered the first legislative mandate for federal grants to the states for brownfield programs and permitted use of grant funds for insurance. Many states have responded to this opportunity.

5.41 Delaware

Like many other states, Delaware has been actively refining and upgrading its brownfields program. The latest modifications were completed through SB 328, signed into law on August 3, 2004.¹⁵ This Act creates a special Brownfields Development Program, provides liability protections beyond the pre-existing voluntary cleanup program, and allows for use of funds from the Hazardous Substances Control Act Trust Fund (originally created exclusively for underground storage tanks) to reimburse allowable costs developers incur for remediation of brownfields. Although these allowable costs are not defined in the Act, it is expected that this language will permit regulations to be written to allow the state to provide financial support for environmental insurance.

The Governor established an internal work group in late 2003 to research state-sponsored environmental insurance as an incentive in the Delaware Department of Natural Resources and Environmental Control (DNREC) brownfields program. The work group is directed out of the Governor's Office and includes DNREC representatives and staff from the Economic Development Department.

DE Rep: We've been in research mode for over a year now, making determinations on what would work best for Delaware. We have issues specific to groundwater and, in the last three months, we've been examining Wisconsin's insurance program centering around groundwater contamination and liability.

Unlike Wisconsin's coverage for its own liability in approving natural attenuation responses, however, Delaware seeks to provide coverage for developers and those willing to risk their capital on brownfield sites. Massachusetts' success also has been a major influence, although the Delaware conclusions about decreasing program participation accompanying decreasing subsidies in Massachusetts are faulty according to reports from BRAC personnel:

DE Rep: We actually started by looking at BRAC. I understand their coverage has changed because of some budgetary issues and they've decreased the actual percentage they're willing to buy down so they've obviously noticed a drop-off in interest in their insurance. But I think the returns on their investment by offering insurance have been marvelous.

The Delaware investigation is pursuing two tracks simultaneously:

DE Rep: The first track, which is really the focus, involves figuring out how we can create more incentives with insurance to increase private developments. The other track involves determining how we can assist the state in mitigating our risk and liability for orphan sites.

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<www.legis.state.de.us/LIS/LIS142.NSF/93487d394bc01014882569a4007a4cb7/47e49d034aae0f5885256ea700747010>

Overall, Delaware's focus, unlike that of Massachusetts, California, and Wisconsin, is more on large sites and major turnarounds than on state support for small redevelopments. Decisions are expected by the end of 2005, at which time the state will announce whether or not it wants to provide an insurance subsidy and what avenues it intends to pursue in further exploring insurance.

5.42 Rhode Island

In June 2002, the Rhode Island legislature passed legislation¹⁶ requiring that the state's Economic Development Corporation and the Department of Environmental Management submit a joint report to the General Assembly by December 2002, recommending methods of ensuring that the state's brownfield projects have access to environmental insurance at reasonable costs. The legislation mandated that the report include a determination of whether or not the state should seek funding to purchase insurance, develop a risk-sharing pool, an indemnity pool, or other insurance mechanism to provide financing for remedial actions. It also required that the report include an evaluation of options for providing CC coverage at affordable rate to projects with cleanup costs under \$1 million.

The requisite report was filed in November 2002. Unfortunately, some of the information it contains is misleading (e.g., referring to BRAC policies as portfolio policies and over-stating the promise for brownfields self-insurance 'captives').¹⁷ No specific recommendations for providing CC policies for small-scale remediations were provided. The primary recommendation involves selecting an environmental insurance broker and referring parties seeking insurance to the broker. An alternative approach that would not estrange the brokerage community would be to provide developers with the qualifications of a set of brownfield brokers. This was not presented, however, on the assumption that a single broker would somehow be able to negotiate volume discount prices from all carriers.

To our knowledge, no action stemming from the report has taken place. Rhode Island revised its brownfields-related legislation in July 2004, repealing the original call for the study (which had been completed), formally assigning the Department of Environmental Management all responsibility for coordinating efforts to facilitate brownfield redevelopment, and giving engineers special access to private sites for assessment of contaminated conditions. The legislation did not mention insurance.

5.43 Vermont

In June 2004, Vermont legislation created an Office of Land Recycling within the Agency of Commerce and Community Development.¹⁸ The bill directs this Office, in conjunction with the Agency of Natural Resources, to develop a brownfields reclamation program that will conduct a prioritized inventory of brownfields and develop strategies for reclamation of the sites.

¹⁶ <<http://www.rilin.state.ri.us/statutes/title23/23%2D19.14/23%2D19.14%2D5.1.htm>>

¹⁷ See Chapter 5.0 in the *Models* report for discussion of the problems with captives.

¹⁸ <<http://www.leg.state.vt.us/docs/legdoc.cfm?URL=/docs/2004/bills/intro/S-042.htm>>

It also requires the Office to form a working group consisting of representatives of financial institutions, hazardous materials management specialists, and insurance carriers to facilitate the availability of insurance products that enhance the feasibility of brownfields. A report is scheduled to be submitted to the General Assembly in 2005.

5.44 Virginia

Virginia's Brownfield Restoration and Land Renewal Act of 2002 directed the state's Department of Environmental Quality (DEQ) to evaluate options for providing low-cost insurance to protect developers from third-party claims from neighboring property owners caused by pollution conditions. Subsequently, DEQ submitted a report in November 2002.¹⁹ The report commented on the advisability of possible options for state-supported insurance.

One option considered was a state subsidy for a portion or all of premium costs. This was not recommended because it posed open-ended liability for the state, given that the universe of brownfields is not known. The report also noted that an open-ended subsidy might not lower insurance costs to covered parties, but could encourage higher premium charges, with the new costs transferred to the state. A second option considered was to pre-negotiate rates and coverages and let the insured pay the entire premium. While this was discussed as valuable in that it could save developers time, the report noted that pre-negotiated coverages would not suit each brownfield project. Some projects would be too risky to insure and the option would likely only benefit "insurable" properties.

The report concluded that insurance is a valuable and effective tool, but did not recommend pursuit of a state insurance program. This recommendation resulted from the conclusion drawn that, in order to be truly effective, such a program needed to provide a subsidy, and the state's budget conditions did not permit that course of action:

VA Rep: What we had ascertained from those who knew the Massachusetts program was that, to be effective, the state had to pay for premiums or deductibles. So that precluded us from evaluating it further in light of the fiscal constraints we had at the time.

Although examination of insurance was put on hold after the 2002 report was issued, DEQ began the investigation again at Brownfields 2004:

VA Rep: That report was a snapshot in time considering our fiscal constraints, and those might be loosening. And, of course, there are more models now than there were two years ago. We spoke with insurers at the brownfields conference in St. Louis and we plan on having additional conversations. The leveraging that occurs with an incentive like environmental insurance is very encouraging and exciting.

¹⁹ <<http://www.deq.virginia.gov/regulations/pdf/bfinsurance.pdf>>

As of fall 2004, DEQ personnel foresee the possibility that insurance will be discussed in General Assembly sub-committee meetings within the next year. The issue of whether or not state-funded subsidies should be provided will be discussed.

5.5 Additional States Investigating Insurance

The states described below are those jurisdictions that have communicated with the authors about environmental insurance or have otherwise exhibited exceptional interest, although they do not yet have detailed plans for programs. Undoubtedly, a survey of all states would uncover states in similar stages with respect to consideration of a state insurance program.

5.51 Indiana

The Indiana Development Finance Agency (IDFA), which has long collaborated closely with the state's Department of Environmental Management (IDEM) in promoting brownfields redevelopment, recently started to accumulate information about environmental insurance. Two staff members from IDFA contacted the authors in the summer of 2004 to collect documentary material and examine efforts by other states to implement insurance programs.

IDFA is undertaking the study and initial planning effort on its own, expecting IDEM and the Indiana Department of Commerce to become involved at the legislative stage and thereafter. The rationale for pursuing insurance is "simply to inject another resource into the state's collection of incentives for brownfields redevelopment." It is anticipated that the initial implementation will be on some form of project-specific basis, with the state subsidizing premiums for coverage, providing that the market offers the products needed at cost-effective prices. The program anticipates providing the full range of insurance that possibly could stimulate redevelopment. Legislative action is required to permit IDFA, which now provides financing support only to public entities, to also offer direct subsidies to private brownfield redevelopers.

Anticipated next steps include meetings with brokers and underwriters to explore possible program concepts. IDFA would administer the program along with its other financial tools, with an insurer or broker selected through a RFQ/RFP process. Legislation both to specify insurance as a form of brownfields assistance, and to authorize direct IDFA assistance to private sector parties, will be pursued in the 2005 legislative session, with implementation targeted for July 2005.

5.52 Wyoming

The Wyoming legislature did not mandate the state's first Voluntary Remediation Program (VRP) until 2000. It has moved rapidly since that date to develop its program. In the summer of 2004, the Department of Environmental Quality, which houses the VRP, let a contract for assistance in program development and promotion, utilizing EPA 128(a) grant funds provided to the state.

One of the five tasks assigned to that vendor as part of a multi-year contract is the conduct of a study and provision of recommendations on the possible uses of environmental insurance for landfills and the potential of state-facilitated insurance acquisition as a means of encouraging participation in the VRP. The Department sees its new brownfields program not as an isolated initiative, but as part of an ongoing, broader charge with respect to contaminated land management. The insurance investigation calls for completion of an assessment of the current environmental insurance market by the end of 2004, followed by contacts with the industry about options available, and the completion of a report to the state early in 2005.

5.6 States that Considered Insurance but Decided Against a Program

5.61 Florida

Florida's Department of Environmental Protection (DEP) was influenced to pursue a brownfields insurance program by the Massachusetts' BRAC program and by presentations at the national EPA meetings. In December of 2001, they convened a day-long open forum to discuss such a program. Attendees included DEP staff, insurance brokers, representatives of the major brownfield lenders in Florida, economic development agency personnel, EPA pilot representatives, lenders, developers, and attorneys.

That forum and subsequent discussions resulted in a proposal for a pilot program that would subsidize insurance premiums by 50% from state funds. The concept involved creation of standardized PL, CC, and SL policies. Insurers would compete to offer individual policies. (Lack of competition in the Massachusetts program was perceived as a drawback.) Financial institutions would market the program and roll premiums into their brownfield loans, to avoid burdening developers with additional paperwork for the coverage.

In 2002, DEP requested \$350,000 for the pilot from the state legislature. They were denied, however, in light of the state's financial situation. In 2003, DEP considered, but decided not to use EPA grant money for the pilot program. The decision was based on an informal telephone and email survey of representatives from local governments, the Governor's Office of Economic Development, a quasi-governmental state economic development corporation, attorneys, environmental consultants, and others. Responses led to the decision to use the federal grant for other purposes:

FL Rep: We did the survey to ask about interest in establishing a pilot program to help offset the cost of environmental insurance and it was an overwhelming non-issue for people. They would rather see the limited money we had for a state response program spent for actual cleanup or site assessments.

There were no further discussions in 2004 about a state insurance program. Neither private developers nor public sector actors had come forward to express a need for brownfields insurance. DEP continues to use EPA funds for site assessments and source removals.

Several factors influenced the decision to not pursue an insurance program further. Most of the concerns were the same as those expressed by discussion participants in Colorado. First, given changes in the state's budget conditions post 2001, funding for a subsidy program in the near future was perceived to be highly unlikely. Second, as indicated above, insurance was not perceived to be a high priority for fund use compared to remediation activities.

Third, even if the insurance program marketing and direct management was to be delegated to brownfield lenders, DEP would have to hire staff or develop the expertise to manage the program.

FL Rep: We have the infrastructure already in house to do site assessments and removals. We don't have to set up a new layer of administrative oversight to do that, which we would have to if we went forward with insurance. It's just one stumbling block, but personally, I wonder whether a regulatory agency should be involved with insurance.

Finally, a primary concern in the state is the cleanup and redevelopment of small-scale brownfields and CC insurance was not available for the sites:

FL Rep: We reached the decision that the present market conditions for environmental insurance were just not there for the types of small sites we deal with. The premiums or the self-insured retentions were just too high. The large development projects were going forward without it or they were building it into overall costs.

5.62 Minnesota

The state of Minnesota is included here as an example of a state where insurance as a brownfields tool was dismissed after only cursory consideration. In 2002, the state's Voluntary Investigation and Cleanup (VIC) program staff conducted a program assessment that entailed a survey to environmental consultants, attorneys, and local governments representatives. Telephone interviews then were conducted with brownfield program personnel from other states. Finally, a focus group was held with a small group of knowledgeable people to finalize recommendations for program enhancements.

Environmental insurance, in fact, was not on the VIC staff's agenda prior to the evaluation. The focus of the survey was privatized versus non-privatized voluntary programs; questions about insurance were not included. The topic only arose in the focus group where one discussant was strongly in favor of pursuing insurance as a risk management tool, while another expressed the opinion that insurance was already being purchased for large projects without government help and was not cost-effective for smaller sites. The majority of participants agreed with the latter speaker. Although VIC staff have attended presentations about insurance since then, they have decided not to pursue it further.

5.7 Commentary

More than anything, this brief review of states considering brownfield insurance programs points to the need for information dissemination and communication among states. States discussed here and, most likely, other states throughout the country are starting from scratch in their considerations of a program. This starting point necessitates a lengthy period of investigation that usually begins at the very basic level of gaining an understanding of the products and what they can do. Most working groups referenced in the chapter have very undefined conceptions about the nature of a state program that would best fit their needs. When the vision is more defined, the experiences of predecessors implementing a similar approach may not be fully explored before action is taken, as in the case of Pennsylvania where pending legislation mimics legislation that has been problematic in California. Some decisions, that may or may not be accurate, have been made based on assumptions that have not been founded in systematic examination of the issues. An example is the conclusion drawn by Colorado, Delaware, Virginia, and Florida representatives that, to be effective, an insurance program must provide subsidies. In Chapter 6.0, we discuss benefits of programs that do not offer subsidies.

Of the eleven states discussed in this chapter, representatives of three – Florida, Connecticut, and Minnesota – concluded that there is little need for an insurance program organized by the state. Similarly, Colorado stakeholders determined that an insurance program involving substantial resources would not be the best use of limit funds and personnel resources. Florida's conclusion, based on an informal telephone and email survey, was tied to the goal of facilitating the cleanup of small-scale projects, for which CC coverages are not available. The same problem was central to Colorado's determinations about the utility of a state program.

In the case of Connecticut, the finding pertained to specific conditions associated with DECD projects, including concerted oversight by the state's regulatory agency. However, the number of brownfield projects utilizing insurance in the Massachusetts BRAC program provides evidence of the need for insurance for projects outside of programs such as the DECD's.

Minnesota's decision to decline further serious investigation of insurance was based on one focus group discussion. It may well be the case that examinations of insurance programs resulting from gubernatorial and legislative mandates will result in more in-depth assessments of both the merits and drawbacks of state insurance programs.

The puzzle faced by states contemplating a state program is that demand for a program is difficult if not impossible to determine prior to establishing the program. The demand that may be invisible or non-existent before a program is developed, may emerge after it is established and the insurance products it offers are publicized, i.e., if you build it, they *may* come.

The chapter that follows addresses the issue of a state program's ability to generate brownfield cleanups and redevelopments. Other issues expressed by individuals developing insurance programs and those managing existing programs are examined.

Chapter 6.0

Discussion

This chapter brings together a number of issues that have emerged throughout previous chapters. It begins with the most basic question – for which there is no complete answer – how can state representatives determine if an insurance program will stimulate brownfields redevelopment better than other brownfield incentive tools? We then address concerns expressed about the programs, beginning with problematic aspects of CC, PL, and SL products. This is followed by a section that discusses the benefits of a state insurance program that does not offer subsidies and examines issues pertinent to such a program, including the need to modify pre-negotiated policies, lack of means to verify premium price reductions, and the ways in which a program may generate volume by encouraging developers to become involved with brownfields.

Section 6.2 raises the issue of whether or not multiple insurers should be included in a program and points to the difficulties involved in structuring a program that utilizes more than one insurer at a time. Section 6.3 addresses optimal ways to develop a state program drawing lessons from the experiences of Massachusetts, California, and Wisconsin. Topics discussed here include the nature of legislation that enables a program, the role of competition in procuring an insurer, making plans for program administration, and determining the parties that should be involved in program development. The report ends by emphasizing the changing nature of the brownfields insurance market and outlining a proposal for a new, untried model for a state brownfields insurance program.

6.1 Deciding on an Insurance Program in the Context of Other Brownfield Tools

State budgets are limited and support for brownfield redevelopments cannot be open ended. The demands for remediation project subsidies will exceed the budgetary capacities of states trying to promote regeneration. This is the context in which decisions on whether or not to undertake plans for an insurance program must be made.

The fundamental problem is *not* whether an insurance program can facilitate redevelopments. The question is, what is the best use of state funds to support brownfields, given the state's policy priorities with respect to cleanup and redevelopment of abandoned and underutilized sites? What is 'best' may be defined differently from state to state in terms of what is most cost-effective, most helpful to small sites, produces the greatest leveraging of private sector funds, etc. The decision-making logic, however, is constant – the 'opportunity cost' approach of economics. That is, it is not a matter of how much you get for spending money for a given policy, but what you give up in results from an alternative use of funds. In order to decide whether or not a program is worth the cost, decision-makers need to know what could have been produced if funds were spent on some other type of support.

Informing a decision on an environmental insurance program using an opportunity cost approach involves addressing two distinct issues, each of which we briefly examine here. First, what are the alternative forms of support for brownfield projects that could be funded? Second, to what extent will help with insurance do more than other support in terms of generating investment that otherwise would not take place?

6.11 Brownfield Project Support Alternatives to Insurance

The two major sources of uncertainty in a brownfield project (other than those associated with the risks of any real estate transaction) involve, first, the cost of a cleanup, since there is always the danger that undiscovered contamination will be found in the course of a mitigation, and, second, the environmental liability that may arise from damage done by the pollution. Once a project is past the remediation stage, the major non-market risks involved are those related to future environmental liabilities. Most of the states' voluntary cleanup programs have focused on relieving the uncertainty associated with these liabilities. State economic development agencies also may provide subsidies to brownfield investment projects.

A general principle of investing is that even exceptionally high risks may be worth taking if there are sufficient rewards for accepting them. Brownfield redevelopers talk about the 'risk premium' they expect to earn on their high-risk investment. A cash subsidy to a brownfield that does nothing to relieve risks can contribute to this premium. Policies that reduce risks may not add dollars to the return on investment, but may attract investment by reducing the risk premium demanded.

Whether both risk reduction and a contribution to increasing investment returns are needed to promote a brownfield redevelopment will depend on the economics of each individual project. It is possible to over-subsidize, spending more to generate a private investment than is needed.

Any assessment of the value of an insurance program thus must be undertaken with an understanding of the broad array of other support that might be available. That support can take a number of forms, summarized in the list below:

- Risk and Uncertainty Reduction
 - Site assessments – to provide developers information on site conditions and reduce the need for them to spend time and money determining how much site mitigation will cost.
 - State-issued assurances such as No Further Action letters and Covenants Not to Sue – to assure developers that a cleanup that meets state mitigation standards will protect them from further state claims for action.
 - Third party liability relief – to assure developers that complying with state requirements will protect them from private lawsuits in state courts.
 - Regulatory decision certainty – to reduce developers' risks by providing clear mitigation standards and time limits for regulatory decision making.

- Financial Subsidies
 - General funding – grants or low-interest loans to investors taking on brownfield projects.
 - Tax credits – permitting developers to write off certain brownfield costs, especially those associated with mitigation, against taxes they otherwise would owe.
 - Targeted subsidies – for specific actions such as assessments, mitigations or the acquisition of insurance, which reduce total costs and reward desired investor behaviors.
 - Regulatory facilitation – providing relief from certain regulatory processes, or assuring expedited action, to reduce the time and money costs of compliance with requirements.

Another possible state action, public remediation of site conditions, can both eliminate uncertainty in mitigation expenditures and reduce developers' actual costs.

Beyond direct financial support to private developers, a state also can stimulate redevelopment by strategically assisting local and regional capacities to promote brownfield investments. The economic returns to regeneration often are felt most strongly at the local level, but not all governments understand how to stimulate brownfield investment activity. As one state environmental agency official acknowledged, "The local redevelopment agencies are the ones in the trenches. Devoting staff to assist them in getting regulatory clearances seems to me to be the most effective use of state government resources. I've got communities that don't even know how to start that process."

The importance of supporting local capacity rises with the extent to which a state is concerned with reclamation of small brownfield sites. The smaller the parcel of land, the more likely it is that a prospective redeveloper will be a small organization, minimally capable of dealing with state regulators and reliant on local support when undertaking a brownfield project.

6.12 Determining if Public Support Causes Private Investment

Does public support generate new private investment? While economic development program managers tend to lay claim to large impacts, linking any specific public sector intervention to a particular private investment has always been extremely difficult.

A project completed with public assistance may have been so attractive to developers that no support was needed; the investment would have occurred regardless of what the state did. The impact of state action in this case would have been zero.

New tax revenue and job creation predictions for prospective projects are based on assumptions made about a private firm's success in the marketplace. Since business privacy is respected under constitutional provisions, the extent to which any one subsidy makes the difference in an investment is impossible to determine objectively. Therefore, in the absence of good data on real impacts, the common measure used to determine the success of a state or local economic development program is the ratio of private dollars invested to public dollars spent on the project – the 'leverage ratio.' This measure merely *assumes* that the public spending produced the private response. There is no solid basis for the assumption.

Determination of the contributions of insurance to the likelihood that any one brownfield project would proceed depends on a number of factors. For example, the value of insurance will depend on other state brownfield policies and practices (e.g., in a state with vague cleanup standards that makes it difficult to get assurances about regulatory mitigation approvals, insurance may be more valuable than in a state that offers well-defined standards). The value of insurance may well depend on market conditions under which a brownfield project is undertaken: high risks are less of a deterrent in a booming real estate market than in a stagnant or declining one. The presence of very strong governmental and/or community support for a project may decrease general investment uncertainties to the point that environmental risks decline in importance and insurance becomes less valuable.

In some instances, however, public involvement may be the key to making a private project go forward, permitting an investor to do something that might not otherwise be possible. A loan guarantee that leads a lender to offer funds that otherwise would be inaccessible is one example. Similarly, when different parties to a possible deal perceive different levels of risk, environmental insurance can facilitate investment in a project that would not take place in the absence of the risk transfer and uncertainty reduction that insurance can provide.

Proponents of local economic development efforts and those that study these efforts have been trying for decades to measure the impact of public support, but have had very limited success. Any study of the issue has to rely on information volunteered by the developers themselves. They, in turn, are motivated to claim that *any* support is essential to attracting their investment, since that claim may generate support that adds to their bottom lines. Accordingly, developers' ratings of different forms of public project assistance often indicate that almost all types of support are 'essential.' Studies going back decades produce the same results. In rare instances in which developers are asked to rank order types of support from the most to least important, not surprisingly, grants top loans, which top delayed tax breaks, which come before various non-cash assistance, generally reflecting the time value of money and certainty of receipt of the incentive.

EPA recently supported one study that avoided developers' strategic responses to research questions. The survey involved asking developers to choose between different bundles of incentives that were intended to attract them to a hypothetical brownfield investment.²⁰ The findings, based on a 2004 survey of developers who were members of the Urban Land Institute, suggest that risk control, including use of insurance, may be the most cost-effective stimulus to brownfields redevelopment. The incentives offered to developers in the study included avoiding any risk of cost overruns on site mitigation as well as any risk of environmental liability claims after redevelopment in addition to cash subsidies and other facilitation. Developers considered complete risk avoidance to be extremely valuable. Considering a project worth between \$20 and \$25 million, for example, complete cost overrun protection was valued at 3% of project cost, or around \$700,000, while complete assurance of no toxic tort claims and the other protections from pollution liability was valued at over 4% of project cost, climbing to the \$900,000 level.

²⁰ Meyer, Wernstedt & Alberini. 2004. "In Practice: Brownfield Relief." *Urban Land*, July, pp. 28-30.

These stark findings and high values, however, are based on a promise that no voluntary cleanup program – or insurance program – can possibly offer: a *guarantee* of *full* liability relief. In other words, we don't know what assurances that fall short of a guarantee are worth, if anything. The combination of voluntary cleanup program protections plus insurance to protect developers might come close to being as attractive as a guarantee. Moreover, the responses come from a group of developers who were interested enough in brownfields to participate in the survey. We cannot tell from these results what those many developers who have not yet tried to undertake a contaminated land project think about the various incentives intended to attract them to brownfield projects.

This discussion of the limited information we have on which investment incentives really work demonstrates there is no general quick fix or panacea to the brownfields problem. Policy makers need to work out the approach that works best in their real estate market conditions. Risk management support with insurance assistance such as subsidized premium costs, pre-negotiated coverages, assistance with insurance negotiations, etc. is, however, likely to be part of the stimulus mix that will be needed to provide the risk-reward balance essential to attracting developers and investors to brownfield redevelopment projects.

6.2 Concerns and Considerations

Section 6.2 addresses concerns expressed by brownfield working group members about state insurance programs. We begin by discussing problematic aspects of CC, PL, and SL products, then turn to issues that are key for those states considering the merits of a program that does not offer subsidies. The section ends with an examination of the problems involved in structuring a program that includes multiple insurers, given the current state of the brownfields insurance market.

6.21 Small Sites and Cost Cap Policies

Perhaps the most common concern about brownfields insurance products voiced is the lack of affordable CC policies for small-scale projects. Facilitating acquisition of the policies is an important goal for the FAIR program in California. The inability to provide them was key to the decision in Florida not to pursue a program and the concern was paramount in the Colorado discussion groups.

In Massachusetts, one of the primary reasons the current carrier was selected was because the insurer was willing to offer a CC product for cleanups under \$1 million. The policies, however, are expensive for most small projects (e.g., for a \$100,000 cleanup, with \$100,000 policy limits and a 35% SIR, the insured has to spend \$152,083 before the policy pays, even with the BRAC 25% subsidy). Insurers have not been receptive to suggestions that they offer CC at lower prices if a state guarantees payment for a certain amount of losses on small-site CC policy claims. One major insurer argues that CC policies in general only add complications and expense and so are not worth inclusion in state insurance programs.

No solution to this problem under existing program structures currently is available. There is, however, a local government strategy for which state personnel may wish to offer assistance. That is, a local government, redevelopment authority, or private developer (possibly a “master developer” selected by a RFP/RFQ process for a targeted area) could acquire title to several small brownfields and place them in a portfolio insurance policy. Such a policy has an ‘aggregate limit’ or the most it will pay for all losses across all properties in the portfolio. By pooling the sites, the minimum threshold for commercially available CC cleanup size could be reached, thus making it possible to purchase the coverages.

This approach, in principle, should lower the premium for the aggregate coverage provided because the underwriter would be spreading risk, i.e., losses incurred at some sites would be offset by the premiums collected for all sites. Whether or not the individual sites are too small to qualify for coverage, the portfolio approach can lower the per-site premium for CC coverage since the insurer could place less capital at risk than it would have to commit if it were to insure each site individually. For example, rather than buying a policy for five individual sites – each with a \$1 million limit – the insured could purchase one policy for all five sites with a \$3 million aggregate limit, predicting that not all five projects will have significant losses.

The principal limitation of this model is that the sites all need to be owned by a single entity. The main problem with financially independent entities sharing a policy with a single aggregate limit is the possibility that one or more insureds will exhaust the limit, leaving others unprotected. The portfolio approach is one method that probably requires some public sector intervention – and one that promises a significant reward for such local government involvement.

6.22 Pollution Liability Policy Terms

When the authors conducted the study of insurance products in 1999, the consensus among insurers was that a three to five year PL policy period was typical with ten to twenty years being the maximum. Insurers have not been re-surveyed since that study, but conversations with them indicate that, with the hardening of the market in recent years, periods of one to five years have become typical. It is still quite possible to get a ten-year policy, but, outside of Finite Risk programs, which are not offered under state insurance programs, it is difficult to purchase a policy with a term limit greater than ten years.

This tendency toward shorter PL policy terms has concerned some individuals developing or considering a state program. It may take considerable time for environmental conditions to generate impacts and third party claims for bodily injury and property damage. Keep in mind that a claim on a PL policy must be made against the insured and reported to the insurer during the policy period. This can be problematic if damage only becomes evident toward the end of the term and the claim is not made before the term ends.

PL policies typically do include an automatic extended reporting period (e.g., for 60 days) in which a claim may be reported to the insurer and carriers offer an optional extended reporting that may be purchased. An insured also may buy a renewal endorsement for a finite period or a ‘rolling’ renewal endorsement (e.g., on a five-year policy, a buyer can renew after one year, so that they always have five years of prospective coverage).

One point to keep in mind is that paying for a policy period longer than five years can be expensive and may turn out to be unnecessary for all brownfields. The loss experiences of insurers indicates that problems at a brownfield site are likely to be discovered within the first five years:

Insurer: We've had ten-year policies available for almost ten years now and we've found that the vast majority of losses come within the first two to five years because that's when you're starting to overturn soil.

Insurer: The value of the policies is that they get the transaction done. You're satisfying a buyer who's willing to take on the risks of a brownfield and the seller who doesn't want the property boomeranging back because of unanticipated environmental problems. If something is going to go wrong, you're going to notice it at the beginning of the term when you start to move dirt.

Thus, while there are advantages to longer policy terms, there are disadvantages as well. Renewing a policy sometimes may be preferable to a longer periods. While claims filed during the policy period may result in denial of renewal or increases in the costs of the renewed policy, if losses have been low and few claims have been made, then the renewal premiums may decrease. Moreover, the insurance market, like many others, tends to run in cycles from a ‘hard’ market favoring insurers to a ‘soft’ market favoring insurance purchasers. Thus prices for the renewal may drop within a few years if a project is undertaken in a hard market.

6.23 Consequences of Secured Lender Policies

Although some insurers have stopped offering SL coverages because of losses incurred from claims, the coverages are still on the agenda for the programs in Massachusetts, California, and Pennsylvania and are being considered in other states. The most important benefit of SL policies is that they provide comfort to lenders and increase their willingness to provide capital for redevelopments that might not otherwise be supported. The 1996 Asset Conservation, Lender Liability, and Deposit Insurance Protection Act (or Lender Liability Act) amended CERCLA by addressing critical lender liability concerns (e.g., by specifying actions lenders can take to avoid federal liability as owners if they foreclose). However, lenders still face important environmental risk exposures that SL policies address (e.g., borrower default due to cleanup costs, diminution of collateral property value due to pollution, and the costs of toxic tort claims should a lender foreclose).

While SL policies increase lenders' willingness to offer brownfield loans, there are important considerations that should be taken into account by public entities with respect to the impacts of the

policies. One problematic aspect of the policies concerns the conduct of site assessments. When they were first offered in the mid- to late-nineties, insurers encountered difficulties marketing the policies because lenders were reluctant to require their borrowers to pay for the insurance while other lenders were not. Consequently, insurers began marketing SL coverages as alternatives to Phase I site assessments. While not all lenders adopted the practice, many did so because of the benefits of the policies. In addition to protecting the lender, having the borrower pay for the SL coverages rather than paying for a Phase I could provide competitive advantages to the lender (e.g., the policies generally cost the borrower less than a site assessment and take less time to process).

If the coverages are purchased, the insurer conducts the due diligence. While insurers still generally require at least a Phase I assessment for large loans in order to issue a SL policy on a single site, some underwriters require only database searches and screening questionnaires for groups of sites in loan portfolios. Phase I assessments certainly are not infallible, but the exceptional risk of providing coverages based on these less intensive investigations has been brought home by the losses incurred by insurers on the policies. The practice also is problematic for property owners because it is in their best interest to understand environmental liabilities stemming from ownership of a property. From the community's perspective, proceeding with a redevelopment project without adequate information about contamination poses a potential risk to human health and the environment because the pollution may not be fully discovered and addressed.

A second consideration with respect to SL policies concerns the ways in which policy payment provisions affect the likelihood of cleanups occurring. Since their inception, SL policies have differed. Some have had provisions that reimburse a lender for the *outstanding loan balance* when a borrower defaults and a pollution condition is present. Others reimburse the lender for *the lesser of* the outstanding loan balance *or* the estimated cleanup costs.

A lender protected by a policy that pays the outstanding loan balance has an incentive to accept the insurer's payment and abandon the property. This leaves a contaminated site for which the availability of capital for cleanup is doubtful.²¹

The same scenario is likely if a lender is protected by a policy that pays the lesser of the outstanding loan balance or the estimated cleanup costs *if* the loan balance is less than the cleanup costs. If the cleanup costs are less than the loan balance, then the mortgagee may take title and conduct a cleanup, depending on the property's expected sale value.

A higher probability of a cleanup exists when a lender has been added to a borrower's PL policy through a mortgagee assignment endorsement like the one currently in use in the Massachusetts BRAC program. This endorsement automatically converts the borrower's PL policy to the lender on

²¹ This policy was offered under Massachusetts' BRAC program until the summer of 2004. However, this negative scenario never occurred under BRAC; there were no claims on the BRAC SL policies, all of which were underwritten individually. Given losses incurred by insurers on SL policies written on an 'outstanding loan balance' basis, it is likely that only 'lesser of' policies will be issued in the future.

foreclosure. Since the PL policy pays for the cleanup, taking title and preparing the site for redevelopment will be the best alternative for the lender and the community. An additional advantage of the endorsement is that it usually can be added to a borrower's PL policy at little additional cost.

6.24 Considerations Relevant to Programs that Do Not Offer Subsidies

Representatives from brownfield working groups in several states maintain that fiscal and political conditions in their states would not permit the use of state funds for insurance program subsidies and also have determined that federal funds should be used for other purposes such as targeted site assessments. Those developing the California and Wisconsin programs are proceeding on the premise that a state program *without* subsidies will provide sufficient incentives to spur brownfields redevelopment.

In addition to the general risk transference benefits of brownfields insurance, the anticipated benefits of a state program, even in the absence of subsidies, include the following:

- Use of a pre-determined PL pricing schedule helps a developer to assess the financial feasibility of a project without the cost of insurance negotiations.
- CC for small projects is made available (often as a condition set by the state selecting an underwriter), although as we have discussed, the policies are not cost effective for most small projects.
- Marketing of the program by the state department or agency administering it serves to educate people about insurance as a brownfields tool – and, more generally, about the prospects for profitable investment in brownfields.
- Pre-negotiated policies save the insureds legal expenses and time tailoring policies.
- Insurance is offered under state programs at reduced premium prices.

In this section, we discuss issues relevant to the last two benefits.

6.241 The Value of Pre-Negotiated Policies. The use of policies that have already been developed is considered a major benefit of state programs. Insurers argue that they lead to price reductions by saving the insurer expenses for manuscripting individual policies and save the insured developers both time and attorney fees:

Insurer: You would be surprised how hard it is to issue a policy. When we have a pre-negotiated policy, it saves us time and money and we pass on those savings.

Insurer: The pre-negotiated policy is a good idea because, first, state programs tend to deal with smaller projects that don't require as many changes as larger ones. Second, the success of a statewide program is going to be based on the volume of deals that are done. If a policy with standard language can be negotiated, it not only helps projects to get started, but also helps the insurer move applications through the process more quickly and easily.

For developers who can't afford specialized legal counsel, this advantage is particularly valuable:

CA Rep: Manuscripting a policy can be very challenging legally and it's resource intensive. The question is, can we focus our program on a niche in the market that is intimidated by insurance and is not currently being reached? Insurers can attract the \$50 million projects. It's the lower band of cleanups where folks don't have the leverage that we want to help with a state program.

However, no two brownfield projects involve the exact same risks and, since the inception of brownfield insurance products, tailoring policies to each project has been understood as a necessity and a benefit of brownfields insurance. After preparing their policies, Massachusetts BRAC personnel soon found that many policies required modifications:

MA Rep: One of the high costs of insurance is manuscripting a policy to the specific needs of the site and state environmental regulations and insurance laws. We constructed user-friendly policies that address most of the risk factors involved in brownfield sites we normally see. We wrote pretty comprehensive policies and thought we had it all covered. But we learned probably a week later that we didn't nearly have it all covered. We now have about forty standard endorsements that we use.

There are two important considerations about which those planning state insurance programs need to be aware. First, even with pre-negotiated policies, additional time, expertise, and expense still may be needed to add endorsements to fit individual brownfield projects. According to BRAC staff, however, these endorsements have not been highly problematic for insured parties. Many of the modifications have been straightforward (e.g., including additional insureds on a policy). Brokers, who must be used to purchase insurance, have been able to identify changes necessary for a particular site and approval of the endorsements by BRAC attorneys has not added time to the policy acquisition process, since the approval is conducted while the insured is waiting for other decisions to be made. Moreover, after the first few years, requests for approval of endorsements beyond those that had already been approved slowed substantially and now largely has ceased.

In Wisconsin, the broker developing the WBIP program is making an effort to incorporate such endorsements into the pre-negotiated policies; those that are not needed for a particular project can be excluded. The extent to which such inclusive policies can be developed remains to be seen:

Broker: I envision a policy that incorporates all the language we think is appropriate for brownfields in Wisconsin. Will there be additional endorsements? Absolutely. But I want to minimize that as much as possible. One of the problems with this concept is the legal review within the insurance industry that a policy like that will take. Insurers have much more flexibility in just endorsing a policy than creating a new form. So, from a functional standpoint, we may not be able to get there.

The second consideration is that some endorsements consist of exclusions the insurer adds to limit coverage because of a particular problem at a site. State program personnel and their consumers need to be aware that, even though a price matrix for coverages may be provided, an insurer under a state program will need to reserve the right to exclude risks perceived to be exceptional. In fact, as has happened occasionally in Massachusetts, the insurer may find it necessary to refuse coverage altogether under the state program for an especially risky project.²²

6.242 Verification of Cost Savings. Premium price reductions rest, in part, on insurer willingness to offer discounts under a state program. Insurers are highly protective of their pricing models, however, and, for proprietary reasons, they do not permit access to their books. How, then, can discounts being offered for policies under state programs be confirmed? This question is critical to California FAIR personnel:

CA Rep: Outside of the subsidy arena, we're still grappling with the role the state will play between the insurer and the insured. If we can't value-add anything here in terms of better premium prices, there's no reason for the state to be in the middle of it.

Unfortunately, there is no way to verify pricing models and discounts in a state-sponsored program:

Insurer: You can't prove that there's a discounted rate. It just can't be done. Brokers can tell you what the prices are, in and out of the program, but that's only anecdotal. But there are actual cost savings plus other advantages to a state program that everybody benefits from.

MassBusiness has had the contractual right to have an auditor review its carrier's pricing models. However, BRAC staff feel comfortable with the pricing they have been receiving in light of feedback from brokers and borrowers who obtained cost estimates before entering the program. An additional consideration with respect to commissioning an audit of an insurer is that, given the highly specialized nature of brownfields insurance, it would be quite difficult to find someone qualified to assess the pricing model who does not already work for a competing insurance company.

6.243 Attracting Enough Projects to a Program. One rationale for the expectation that a state program will receive discounts is that the insurer providing coverages will anticipate a high volume of business from its arrangement with the state. However, stakeholders in several states, including Wisconsin, Colorado, Delaware, and Rhode Island have expressed the concern that, without subsidies, their programs would not be able to attract enough users to achieve sufficient discounts from an insurer to make the program attractive to developers.

There is a consensus among insurers that subsidies *do* permit cost reductions because of an increased volume of sales. One insurer argues that smaller states or states with relatively few brownfields that

²² The issue of policy endorsements becomes especially important when premium subsidies are provided under a program because program administrators need to determine which endorsements are eligible for payments.

believe they cannot offer subsidies should form regional compacts to establish a program that would generate sufficient volume.

Three important considerations, however, should be taken into account before dismissing the possibility of a program on the assumption that a state will not generate sufficient volume without subsidies. First, volume can be generated by (a) program marketing that educates people about insurance as a brownfields tool, and (b) the benefits of policies offered under a state program, i.e., pricing schedules and pre-negotiated policies. It is very possible that the needed volume will be created by the program itself, to the extent that it brings more of the potential smaller developers into the brownfields marketplace:

Insurer: The standardized policy has increased the overall brownfields market in Massachusetts. A lot of smaller developers that have not been playing in the brownfields universe are coming into the program because they've learned about environmental insurance.

WI Rep: There are hundreds of sites in Wisconsin that don't get insurance because people don't understand it or think it's too expensive. If we can set up this program like we want it, we hope that a lot of those people will feel like now there is a streamlined product that meets their needs. We think that there would be a big increase in insurance use.

Second, from the insurer's perspective, the volume of policies sold in proportion to those underwritten is higher within a state program than in the open market. Outside of a program, an insurer may have to underwrite and price many policies for each one that is actually sold. Within a program with published costs for the standardized coverages, the proportion of insurance policy placements per initial inquiry will be much higher.

The third consideration is that the volume carriers anticipate comes from both within and outside of the program. That is, the reduced prices might be viewed to some extent as 'marketing' discounts in that selection of a carrier as a state provider attests to the trustworthiness of the carrier and serves as a means of advertisement for the sale of insurance outside the program:

Insurer: (Being a state insurer) is a great marketing tool because a lot of people don't know about environmental insurance. When the state says here's a tool to use, then suddenly people who weren't buying insurance realize they can pass off the liability they've feared to an insurance carrier. We sell more insurance, so there's volume creation.

In short, it may be the case that some brownfield working groups overestimate the current level of state brownfield activity that is needed to make a program feasible.

6.25 Competition in a Program: Using Multiple Insurers

With respect to cost reductions, two positions have been put forth concerning the use of a single or multiple insurance providers within a state program. Some in the insurance industry and state governments argue that having two or more insurers competing in a program is key to keeping premium prices low:

Insurer: We should extend the free enterprise concept and have more than one carrier involved in a state program. All carriers have coverages they like to do better than other coverages. From the buyer's perspective, you can choose the carrier and the coverage you want.

Others posit that use of a single carrier that receives all of a state program's business is a critical price-reducing factor because the selected insurer is willing to offer premium discounts and types of coverages they would not be able to offer if they were competing with others:

Insurer: A single carrier model has significant advantages. We're able to offer a more competitive approach, including the ability to do cleanups under a \$1 million threshold. We don't feel we would be able to offer them in a multiple carrier situation because we would wind up with all the small cleanups and that's where you see all the problems. We need to spread our risks with bigger cleanups.

Simply offering a subsidy for the cost of a premium from any insurance carrier is not a viable option. Even with competition among insurers, there is no way to tell whether or not the subsidy is driving up the cost of coverage across all insurers, as the premiums charged could rise to the sum of the subsidy and what the market otherwise would bear without the assistance.

At this point, it is not possible to determine whether a single or multiple provider approach actually does result in greater insurance cost reductions since we only have a single-carrier model. A more complex issue, though, given the current brownfields insurance market, is how a multiple insurer program would be structured.

One alternative suggested in California's RFPQ involved selecting multiple providers for the FAIR program. All of the carriers would agree to the same policy wording, terms, and binding processes and would compete with each other for policy placements. This proposal now has been complicated by the withdrawal of some insurers from the SL and CC markets. As we noted earlier in Chapter 2.0, only one of the three carriers interested in the BRAC program offers all three policies.

The concept of having each of these three insurers provide either PL or CC or SL is not tenable because PL is the preferred policy among all carriers and no insurer is willing to offer SL or CC alone. Moreover, in terms of cost reductions, the structure does not make good sense unless an insurance buyer is purchasing only one type of insurance. That is, cost reductions derive from saving the insurer risk assessment costs for each policy written for a brownfield project. For example, under the BRAC

program, a PL policy with a \$5 million limit and a \$10,000 deductible costs about \$30,000 if a buyer only purchases PL, but costs about \$25,000 if the buyer also purchases CC for the same project.

A possible outcome of the current BRAC negotiations is to have all three interested insurers as providers for the program. Each would offer PL and either SL or CC, thus introducing insurer competition into the program.

However, this approach is problematic because, first, relative to the a single provider model, the structure would negatively affect cost reductions because each of the carriers would incur expenses underwriting policies for which no sale would be made. Second, policies offered on a percentage discount basis would need to be uniform for comparison purposes in terms of basic provisions, definitions, etc. and this would entail substantial legal review on the insurers' part. Third, a procedure would need to be devised to determine which carrier is allowed to sell a PL policy in the event that a buyer wishes to purchase all three products.

6.3 Developing a State Insurance Program

There has been significant variation in program creation processes among the states on which this report has focused. Table 6.1 summarizes these differences. It is useful to include Massachusetts although, as we noted in Chapter 2.0, BRAC was not originally developed as an insurance program. The remainder of this section discusses the lessons that can be gleaned from the comparisons.

Table 6.1 Massachusetts, California, and Wisconsin Program Development Comparisons			
	Massachusetts-BRAC	California-FAIR	Wisconsin-WBIP
Parties Involved	State non-gov econ dev org State econ dev dept	State env agency Private consultant	State env agency State broker State risk manager Brownfields Study Group
Program Legislation	Very general. Not intended for insurance program	Very specific	Very general
Bidding Requirements	None for insurer	Required for insurer	None for insurer Broker competitively bid
Insurer Selector	Non-gov econ dev org	State env agency	State env agency State broker State risk manager
Costs to State	\$250,000 Non-gov econ dev org time Econ dev dept time	\$700,000 State env agency time	State env agency and state risk manager time
Development Period	1 year after legislation passed	4 years to date, but delays due to admin change	2 years anticipated

6.31 The Need for Flexible Enabling Legislation

Since its inception, the brownfields insurance market has been dynamic. New coverages become available; other coverages become more difficult or expensive to purchase. Product lines change. In recent years, some insurers have stopped offering CC and some no longer offer SL policies. In addition, state funds available for insurance programs may come and go.

In California, the details in the legislation became stumbling blocks. Definitions of terms such as 'pollution condition' were inappropriate for an insurance policy, the mandate to insure all brownfields was perceived by the insurer to undermine profits from larger projects, and the specified SIR for CC policies placed constraints on the price the insurer could charge for premiums. Moreover, the legislation requires SL coverages that are no longer offered by the provisionally selected insurer.

As representatives from Massachusetts and California urge, the legislation that establishes a program must be flexible in nature to allow for these changes:

MA Rep: A program has to be a living thing. From 1999 to the present, our program has changed significantly. Brownfield issues evolve. Insurance products evolve. We've had to keep pace with that, not to mention the fact that we've had to deal with budget changes that affected subsidies.

CA Rep: The less specificity you have in an authorizing statute the better. A statute's a whole lot harder to change than a regulation or anything else. We pretty much have to live with what's in our statute, unless and until we can get that changed.

6.32 The Role of Competition in Insurer Procurement

Most everyone agrees that the free enterprise principle of competition is a positive driving force. As one insurer put it,

Insurer: The reason that our products are better now than they were ten years ago is that we compete against each other every day. We're forced to be more creative and stretch ourselves in terms of what we're willing to do. That's what has reduced the pricing and made the policies more responsive.

An issue raised by the experiences of the states, however, is how competition should enter into program creation. In California, the enabling legislation required competitive bidding among insurers:

CA Rep: Our selection process was extremely time and resource intensive. The statute required that we conform to a contract procurement process, which added procedures that really didn't fit a program development process.

Rather than competitively bidding an insurer, Wisconsin began by selecting a broker through a competitive process:

Broker: We were selected as the state's advisor on environmental insurance issues. That was a competitive procurement. Then we seek competitive bids from multiple insurers. California went to the insurers first. The problem was, the state was trying to be a broker and they probably didn't know the most effective way to go about getting the best terms and conditions in the marketplace. Now they're at the point where they need a broker. They went about it backwards.

In Wisconsin and California, the competition for a single provider will be reopened every three years. The Wisconsin process differs from California's in that it relies on the expertise of the broker to work with the insurers on program development, negotiate with insurers, and, importantly, assess the merits of the proposals received in order to recommend the best insurer.

6.33 Planning for Program Administration

In both Wisconsin and California, program administration decisions have been left as one of the last considerations, and, as noted in Chapters 3.0 and 4.0, key administrative issues are yet to be resolved. Those considering a state program would benefit from contemplating these issues at an earlier phase in program development, regardless of the extent to which state personnel will be playing administrative roles. Depending on the nature of the program, tasks that need to be considered include:

- qualifying applicants as eligible;
- issuing subsidy payments, if offered;
- marketing the program;
- overseeing or managing negotiations with insurers on a recurring basis;
- collecting and analyzing program evaluation data pertaining to the insurance (e.g., policy dollar limits and premiums, claims payment records, rejections of projects by the insurer);
- collecting and analyzing program evaluation data pertaining to customer satisfaction and to the public benefits that accrue from projects (e.g., cleanup costs, investment dollars in projects, job and tax creation estimates).

Questions that should be addressed include:

- How large of a budget will be needed for program administration? How will these funds be provided?
- Which entity, particularly with respect to economic development versus environmental units, has staff with backgrounds best suited to manage an insurance program?
- If a brokerage firm will manage the program, for which tasks will they be responsible?
 - Will the program rely on only one brokerage firm for administration?
 - How will the broker be compensated for program administration functions?
 - How will other brokers in the state participate in a way that encourages them to bring clients to the program?

6.34 Parties Involved in Program Development

The value to program development of involvement of a multiple stakeholder team is made clear by comparing the experiences of different states. In California, Cal/EPA has led the effort. At the beginning, the staff had little knowledge of brownfields insurance. Although they had hoped for assistance from the state risk manager's office, they found they could not rely on this source for guidance on issues specific to brownfields insurance. Neither did they have in-house legal specialists to help guide the process and negotiate the new policies with the insurer. Consequently, they spent considerable funds for a consultant to assist them. Similarly, Massachusetts found it necessary to pay substantial attorneys' fees for review of their policies.

In Wisconsin, the team consists of DNR representatives, the state's insurance broker, the state's risk manager, and the Brownfields Study Group. The broker has been key in terms of conceptualizing the program and working with insurers. The state risk manager, having been involved with brownfields for a decade, is familiar both with brownfields and insurance products for them. He has played a critical role in working with the broker to conceptualize both of Wisconsin's programs, reviewing the specifications sent to insurers, participating in the selection of an insurer, and winning legislative approval for the insurance programs. The Study Group has made important contributions in terms of providing input from multiple perspectives into the design of the insurance programs, gaining support for the enabling legislation, and providing legal review of the insurance policies.

6.4 Coming Attractions

In this final section, we would once again like to emphasize the dynamic nature of the brownfields insurance market. We do so by concluding the report with a new, untried approach to state programs. The model was outlined by one insurer during the Colorado conference calls in March 2004 in the context of ways to address the problems faced by developers of small-scale brownfields.

6.41 Proposal for a New Approach to State Programs

This approach does not involve CC coverages, but consists of a PL policy to cover previously unknown conditions discovered during remediation and/or redevelopment. It addresses the "what if we start digging and find something else" issue that frequently stalls brownfield transactions.

The concept entails creating a portfolio policy with a large aggregate dollar limit and sub-limits for each project. The insured would be a quasi-governmental organization or unit of the government (other than an environmental regulatory agency that could trigger a claim). Developers would be encouraged to become participants with the status of additional insureds on the policy. Participants could be charged a share of the premium or, alternatively, the state could provide part or all of the premium as an economic incentive. The carrier commonly insures similar large portfolios for companies, such as real estate firms, that own hundreds of sites.

To qualify for the program, an applicant would need a state-approved cleanup plan that would list known pollutants. This condition usually is imposed on insurance purchasers and would not constitute a new or inordinate requirement. The cost of insurance would be lowered because not all sites would be underwritten individually. An audit of a small percentage of the sites would be conducted and applications would be screened to identify sites that might entail exceptional risks for which the insurer would need additional information before binding a policy.

To determine the aggregate limit and premium, a relatively short-term policy could be created initially (e.g., a one-year policy). It would provide sufficient coverage for projects ready to enter the insurance program and also leave room for adding others. In subsequent years, the insurer would develop loss ratios and the state would be able to more accurately predict the number of participants likely to join the program. Policy dollar limits then would be adjusted to assure that the aggregate limit was high enough to provide sufficient coverage for all projects.

The use of sub-limits for each participant would avoid a situation in which one or a few projects used up the aggregate limit. If a developer of a large project requested dollar limits that would jeopardize the participation of small project developers, the aggregate limit and premium could be increased to accommodate the developer. Alternatively, the developer could be denied participation and would need to purchase a policy outside of the program.

The policy would include basic liability coverages that are most commonly needed by brownfield remediators and developers including:

- liability claims for bodily injury and property damage caused by pollution on or emanating from the insured's property;
- remediation of on-site and off-site previously unknown, pre-existing pollution; and
- legal defense costs to defend against third party claims.

Additional coverages such as business interruption or transportation of hazardous material coverages would not be included in the master policy. The insureds, however, would be able to purchase them if needed at reduced costs, since the insurer already would have underwriting information about the projects.

To initiate the program, the state could negotiate the policy, but wait until a predetermined number of users were ready to proceed with the cleanup and/or construction phases of their projects. At that point, the state would pay for the premium and the policy would bind.

Implementing the model would mean procuring funds to start the program, aligning projects to initiate the policy, and marketing the program to developers. Further details about this model need to be developed such as policy renewal provisions, the possibility of including a provision that protects lenders in the event of foreclosures, and the ways in which unknown conditions would be defined.

The approach has the advantages of other state programs including use of a pre-negotiated policy that saves legal expenses and time and a pre-set pricing schedule that helps to calculate project costs. In addition, the model removes the ‘price bias’ that now exists for small projects that want small limits. In the Massachusetts BRAC program, for example, the cost per dollar of coverage for a \$1 million policy is more than double that for a \$10 million policy. With this model, each party would be charged the same per million in coverage. Thus, although all projects would benefit from lower-cost insurance, projects requiring smaller dollar limits would not be charged more per million as they are now.

The critical determining factor with respect to this concept is how much the policy would cost compared to the pricing for PL policies under the Massachusetts and Wisconsin programs. The unfortunate conundrum is, until a state is interested in seriously pursuing the model, the insurer cannot afford the effort and expense of developing the program in sufficient detail to allow cost estimates. However, until the cost estimates are forthcoming, states most likely will not want to undertake the effort and expense to seriously pursue the approach.

6.42 Stay Tuned

As we noted in our opening, this report provides snapshots in time of ongoing processes. Annual summaries of state brownfield insurance efforts will be generated for the next four years, through 2008. By next year’s edition, a number of issues should be resolved. Among others, key questions to which answers should emerge include the following:

- Will the current MassBRAC negotiations result in one or multiple insurers in the program?
- On the basis of feedback from lenders, what will MassBRAC personnel decide about the adequacy of the mortgagee transfer endorsement to borrowers’ PL policies?
- Will Wisconsin’s WBIP program include pre-negotiated pricing schedules? Will the insurer be willing to rely on DNR site investigations to insure sites?
- Will WBIP and California FAIR personnel successfully address program administration issues, including compensating the brokers they foresee managing and evaluating the programs?
- What will be the nature of the risk management education program Colorado pursues, if any? Will the ways in which it is funded and administered suggest new options for other states?
- Will the Pennsylvania insurance bill be approved? Will it correct the statutory issues that have been problematic in California?
- What innovations will emerge from other states as they consider creation of state insurance programs?

Subsequent reports should help refine efforts to assure that publicly supported risk management efforts provide efficient support for private sector brownfield investors. As more states become involved with insurance, and more officials devote time to developing and running programs, their capacity to analyze and compare across programs will grow, so that future reports in this series should rely less on analysis by the authors and more fully incorporate state officials’ perspectives and comparative analyses of their own and other states’ efforts.

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